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IN THE

Supreme Court of the United States

OCTOBER TERM, 1959

No. 405

PAN AMERICAN PETROLEUM CORPORATION, *Petitioner*,

v.

FEDERAL POWER COMMISSION, *Respondent*.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

W. W. HEARD
JOHN F. JONES
Pan American Petroleum Corporation
P. O. Box 591
Tulsa 2, Oklahoma
WILLIAM J. GROVE
CARROLL L. GILLIAM
Dow, Lohnes and Albertson
600 Munsey Building
Washington 4, D. C.
Attorneys for Petitioner

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v.

FEDERAL POWER COMMISSION, *Respondent*.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

Pan American Petroleum Corporation, on its own behalf, and, under orders of the Federal Power Commission and the judgment below, in a representative capacity for sixty-three other persons,* prays that a

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* Episcopal Theological Seminary of the Southwest; First National Bank of Longview, Texas, as Trustee for the Roy H. Laird Memorial Hospital; The Bishop Quin Foundation; the Methodist Home; (successors in interest to Annie B. Laird, Independent Executrix of the Estate of Roy H. Laird, deceased); Texie B. Davis Musser as Trustee for Jack M. Carson, Jr., (successor in interest to W. Dudley Taylor, Jr., Trustee for Jack M. Carson, Jr.); W. Dudley Taylor, Jr., Trustee for Dudley Davis Taylor;

Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the District of Columbia Circuit entered in the above case on June 18, 1959.

OPINIONS BELOW

The Opinion of the Court of Appeals (*infra*, Appendix A, pp. 1a-21a) is not yet reported. The orders of the Federal Power Commission (R. 3432, 3496), are reported at 19 F.P.C. 519.

JURISDICTION

The judgment of the Court of Appeals was entered on June 18, 1959 (*infra*, Appendix A, p. 22a). The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1) and § 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

Rose Rudman, as Executrix of the Estate of I. Rudman, deceased; Janie R. Strength, as Executrix of the Estate of W. H. Strength, deceased; Bracken Oil Company; J. G. Catlett Company; Fair Oil Company (successor in interest to R. W. Fair); Producing Properties, Inc. (successor in interest to Hollandsworth Oil Co.); Rudeo Oil and Gas Company; Sells Petroleum, Inc.; Skelly Oil Company; Strebor Oil Company; Three States Natural Gas Company; Tintic Standard Mining Company; J. G. Barker; C. M. Beckett, Jr.; J. M. Brown; L. D. Brown; W. H. Bryant; Winifred Chapman; H. H. Coffield; J. L. Copeland; Texie Bialock Davis; Sam B. Hall, Jr.; P. W. Hemphill; E. Fred Herschback; Thelma Higgins; J. S. Hudnall; Arch Jarrott, Jr.; L. C. Johnston; Mrs. R. Bruce Johnston; Franklin Jones, Sr.; M. H. Jones; Hobart Key, Jr.; Will Y. Lancaster; C. A. McLean; Roy Marcom; Ralph Massad; A. B. Miller; Morris H. Moore; Mrs. Beulah A. Ostrom; Jack L. Ostrom; Robert R. Ostrom; Bryan W. Payne; Robert B. Payne; G. W. Pirtle; Ernest E. Smith; Summerfield G. Roberts; Alice Snider; D. H. Snyder, III; Frank Davis Snyder; W. Dudley Taylor, Jr.; Winston Taylor; D. A. Thomas; Sam Trant; Lina H. Van Sickle; Paul L. Whaley; Jack Blalock; and C. A. Brian.

QUESTIONS PRESENTED

1. Whether Section 4(e) of the Natural Gas Act and the Fifth Amendment to the Constitution prohibit determination of reasonableness of the price provided in a gas sales contract unless "cost-of-service" studies are presented, (a) where such sales contract is but one of hundreds of a producer's gas sales contracts and prices in other contracts are not in issue, (b) where the one price in issue is received by more than seventy producers who separately make other sales under other contracts not in issue, and (c) where determination of a "cost-of-service" for the one price in issue would require attempted isolation of a "cost" of only a minute segment of the total business enterprise of each of more than seventy producers.

2. Whether the judicial review to which a petitioner is entitled under Section 19(b) of the Natural Gas Act and Section 10(e) of the Administrative Procedure Act of 1946, is denied when a Court of Appeals affirms Federal Power Commission action on grounds advanced for the first time in the Court of Appeals and fails to review Commission conclusions of law as to statutory and constitutional limitations upon its powers under Section 4 of the Natural Gas Act, specifically challenged by petition for review.

CONSTITUTIONAL PROVISION AND STATUTES INVOLVED

The provisions of the Fifth Amendment to the United States Constitution, and the pertinent provisions of the Natural Gas Act, 52 Stat. 821, 15 U.S.C. § 717, *et seq.*, and of the Administrative Procedure Act of 1946, 60 Stat. 237, 5 U.S.C. § 1001, *et seq.*, are set out in Appendix B, *infra*, pp. 23a-30a.

STATEMENT

This case began less than ten months after the decision on June 7, 1954, in *Phillips Petroleum Co. v. Wisconsin*, 347 U.S. 672 (1954), holding that certain sales by independent producers are subject to regulation under the Natural Gas Act (Act).[1] The order under review, raising issues of statutory and constitutional limitations upon Commission power to determine reasonableness of producers' field prices, is the first such order to reach this Court without an order of remand by a Court of Appeals for further proceedings before the Federal Power Commission (Commission).

1. *Factual Background.* Pan American Petroleum Corporation (Pan American) is engaged in production and sale in the producing fields, of oil, natural gas, gas condensate, and other hydrocarbon products. Its domestic production operations are conducted throughout the producing regions of the southwestern, midcontinent and Rocky Mountain states. It makes over one thousand individual sales of natural gas to pipelines and industries in widely scattered fields.

After the *Phillips* decision, several hundred of Pan American's gas sales contracts became subject to the Commission's jurisdiction, but it was permitted by Commission regulations to file only 150 of these contracts (18 C.F.R. 154.91). Each of the 150 separate contracts was filed as a separate "rate schedule" under

[1] As noted in the *Phillips* case, an independent producer engages in exploration for and production and sale of natural gas, but does not engage in interstate transmission of gas and is not affiliated with an interstate natural gas pipeline company (347 U.S. at 674-675).

Section 4 of the Act (R. 287-290).[2] Among these is the contract covering sale by Pan American of its respective shares in natural gas produced from 33 wells in the Woodlawn Field, Harrison County, Texas (R. 2662).

Operations in this field are conducted in accordance with practices and contractual arrangements both typical of and necessary in the natural gas producing industry. One hundred and fourteen persons have acquired the working interests in leases in the field (R. 2438, 2816-21). The 114 persons thus own interests in the gas and other commodities produced in common streams from 49 wells on these leases. Each owner of such an interest is also engaged in various other activities, and most of these persons, like Pan American, make interstate and intrastate sales of natural gas in numerous other fields in Texas and other states (See *e.g.*, R. 741-2, 757, 767, 777). However, the individual interests of these owners in the gas producing wells in the Woodlawn Field vary widely from well to well, ranging, for example, from 91.87% to 0.15% in one well and from 31.76% to 0.63% in another. Some of the producers own an interest in only one or two wells; others own interests in several wells, and still others own interests in most of the wells (R. 2816-21). Under arrangements which are customary in the industry,

[2] At the time of filing, the name of the company was Stanolind Oil and Gas Company. It was then making 1,035 separate sales of gas, of which 701 were under "percentage-type" agreements which are not filed as "rate schedules" under Commission regulations; 184 were sales not subject to Commission jurisdiction; and 150 were sales for which contracts were filed as "rate schedules." After merger with another company in 1957, the name was changed to Pan American Petroleum Corporation. The company now has more than 250 sales contracts on file as "rate schedules."

Pan American, the owner of the largest interests, operates 33 wells under agreements with the more than 70 owners of interests in these particular wells; there being a separate operating agreement for each well. Each owner retains a voice in operation of each well in which he owns an interest. Each owner also has the right to sell his share of gas production, including the right to cancel, on short notice, any sales arrangement made with respect to his gas by the operator. The operator is authorized to sell a non-operator's share only when the non-operator fails to dispose of his share as currently produced (R. 74-75, 120-21).

In April, 1951, Pan American executed a twenty-year contract to sell its respective shares of the gas produced from the 33 wells to an interstate pipeline company, which, even after extension of its line into the field, was, for several years, the only pipeline purchasing gas in the immediate area. Thereafter, the majority of the other owners elected to sell their respective shares under terms of the Pan American contract without formal execution of a separate instrument (R. 73, 107, 231). Under these arrangements, Pan American, as operator, delivers the undivided well streams to the one purchaser, and transmits to each owner his shares of proceeds from the gas sales (R. 107-8, 2805-2821).

2. *The Commission proceeding.* Under Commission regulations, producers who are not signatory parties to a sales contract are not permitted to file a "rate schedule," and the contract which is the "rate schedule" of a signatory owner, usually the operator, is deemed to be that of each of the other owners (18 C.F.R. 154.91). Pan American's contract covering deliveries in the

Woodlawn Field, therefore, is designated "Pan American Petroleum Corporation (Operator), *et al.* FPC Gas Rate Schedule No. 31;" and filings or Commission orders concerning this schedule apply equally to the price received by Pan American and to the price received by each of more than 70 non-operating owners who are *not* permitted to file their own schedules.

In March, 1955, on behalf of itself and the non-operating owners, Pan American filed with the Commission a notice that under the contract the price would increase on April 3, 1955, from 13 to 13.5 cents per thousand cubic feet (Mcf) (R. 2805). On April 1, 1955, the Commission issued an order suspending the increase as a change of the "rate schedule," and directing that a hearing be held to determine the reasonableness of the increase under Section 4(e) of the Act (R. 3069). During the hearing, Pan American and a non-operating producer introduced extensive factual evidence in support of the one price in issue. The producers did not present evidence in the form of the "conventional cost-of-service" used in the past in proceedings where the whole body of rates of a pipeline or utility have been in issue.[3] A comprehensive showing was

[3] The "conventional cost-of-service" concept, under Commission practice, requires the determination of a "rate base" consisting of each individual company's capitalized investment and working capital; the calculation of the company's proper "rate of return" upon its investment in jurisdictional activity; and the determination of the company's annual operating expenses and depreciation and depletion charges, which, with the return on the "rate base" and tax allowances, generally comprise an annual "cost-of-service." These calculations require, among other detailed steps, an allocation of costs directly or indirectly associated with jurisdictional activity, an allocation of general administrative overheads and exploration and developments costs, an allocation of investment and expenses between jointly produced commodities

made as to the impossibility of presenting evidence in the "cost-of-service" form because of the nature of the producing industry, including data as to the number of owners, problems of "allocating" costs to gas produced with unregulated commodities from the same wells, wide variations in total costs of acquiring lease interests, etc. (R. 287, 1276-7, 1286-96, 1300-15, 1842-50).

Before the Commission, the producers argued that in review of a producer's sales price, the Commission was not bound by law to any single rate-making formula or combination of formulae, but was free to devise rate review procedures which recognized the distinctive characteristics of the gas producing industry. The producers also argued that neither the Act, nor constitutional prohibitions against imposing confiscatory rates, required presentation of "cost-of-service" evidence.

On April 14, 1958, the Commission entered an order disallowing the half-cent increase (R. 3432). By adoption of its Examiner's findings, the Commission concluded, *inter alia*, that there was no affiliation between

to attribute a portion to natural gas, determination of tax liabilities and working capital requirements, and analysis of individual "return requirements" which can be based only upon the revenue requirements and earning capacity of all of the company's jurisdictional activities. Evidence submitted by the producers included, but was not limited to, objective data showing the competitive negotiation of the contract price, the commodity value of the gas in the competitive market, statistical analyses of trends in costs and price levels in the competitive market, absence of impact of the increase upon value of the gas to the purchaser and upon a consumer, and other circumstances and conditions surrounding the sale. (See R. 61-65, 72, 76-84, 396, 405-16, 1829-1836, 1870-1892, 2200, 2203, 2221, 2521, 2526, 2527, 3302).

the producer-sellers and the buyer; that the contract was entered into at arm's length in a competitive market; that the evidence indicated that the half-cent escalation would not have a "substantial impact" upon ultimate consumers; that the evidence was such that inference could be drawn that "numerous practical difficulties would accompany an attempt to apply a rate base, cost-of-service formula . . ."; and, that the contract price "falls within the range of prices paid to other producers in the pricing area" (R. 3302-03, 3305-08).

However, the Commission also adopted the Examiner's conclusions of law upon the question of its power (R. 3307-3308):

> ". . . The central issue presented is one of constitutional requirements, and of our statutory power. The Applicants claim that the Act does not limit the Commission to the use of any particular formula or combination of formulae in determining just and reasonable rates under Section 4(e)."

The Commission held that both the Act and the Constitution impose "requirements" that it consider "cost-of-service" evidence, regardless of the scope of the rate inquiry; that because the producers had not submitted such evidence, the record was deficient in terms of both the Act and the Constitution, and it was legally impossible for the Commission to pass upon reasonableness of the contract price; that, by failing to meet this statutory and constitutional "requirement," the producers, as a matter of law, had not shown the price to be "just and reasonable"; and, that, for these

reasons, the contract price must be disallowed (R. 3307, 3308, 3435).[4]

Rehearing was sought under Section 19(a) of the Act, but was denied, two of the five Commissioners dissenting (R. 3439-3453, 3500).

3. *The petitions for review.* Sixty-four non-operating owners and Pan American sought review under Section 19(b) of the Act in the United States Court of Appeals for the District of Columbia Circuit.[5]

The petitioners challenged as erroneous the conclusion of law upon which the Commission's order was predicated—that the statute and the Constitution require consideration of "cost-of-service" evidence. Specific reference was made to Commission error in failing to follow the principles of law that where only one of many of a regulated company's rates is in issue (1) application of the standard of reasonableness is

[4] In addition to the conclusions of law set forth in their orders, both the Examiner and the Commission referred to conclusions of law set forth in Re *Union Oil Company of California*, 16 F.P.C. 100, 110, 111 (1956) which was reviewed and remanded for further proceedings, *sub nom. Bel Oil Corporation, et al. v. Federal Power Commission*, 255 F. 2d 548 (5th Cir. 1958), *cert. den.*, 358 U.S. 804 (1958).

[5] A joint and several petition was filed by Pan American and sixty three non-operating owners. A separate petition was filed by Continental Oil Company, a non-operating owner which, with Pan American, is signatory to the contract. Upon motion by the Commission, the Court dismissed the petition as to the owners who, under Commission regulations, may not file separate rate schedules, on the ground that these owners were not formal parties. As the Commission itself advised the Court of Appeals, the result of this dismissal was and is that while Pan American proceeds on behalf of the other owners in a representative capacity as required by regulation, each and all of the non-operating owners remain bound by Commission orders.

not, as a matter of law, dependent upon consideration of "cost-of-service" evidence, and (2) the company-wide "end result" test of "revenue requirements" or confiscatory rates, cited by the Commission as controlling, is inapplicable. Whether "cost-of-service" evidence would not be required, as a matter of law if all of a producer's sales were in issue, was not before the Court.

The Commission brief did not undertake to defend the legal conclusions which were the sole basis for the order below, although there was no indication the Commission itself had actually abandoned these conclusions. The Commission's brief urged that the Court need not decide whether the conclusion of law (that the Commission had no power to act upon the record) was erroneous; instead, it was argued that the order should be affirmed as though the Commission had exercised its administrative discretion and thereby had concluded that the price was not just and reasonable, *e.g.*:

> "Whether or not the Commission was *required* to hold 'cost' evidence necessary to petitioners' case, under the controlling judicial authorities need not be decided. The fact is, that the Commission *did* so hold, and its refusal to accept petitioners' rates as 'just and reasonable' was an action at least within the scope of its discretion."[6]

It was also argued, just as the producers had urged before the Commission itself, that "[t]here is much

[6] Brief for Respondent Federal Power Commission below, p. 10. Emphasis was the Commission's.

latitude allowed the Commission in its selection of criteria."[7]

4. *The Court of Appeals opinion.* Regarding the issues raised here, the Court of Appeals first assumed that the petitioners were correct as to embodiment of the historic zone of reasonableness in the "just and reasonable" standard, and as to the distinctions between application of that standard to test one specific rate, and the judicial test of barely non-confiscatory or "lowest reasonable" rates. However, the Court then ignored the controlling questions raised by the petitioners and substituted a different question:

> "The question . . . is whether the petitioners' evidence is sufficient to compel us to reverse the Commission's conclusion that the evidence was not enough to sustain the proposed increase."

Brief reference was then made to decisions recognizing the breadth of administrative discretion in rate regulation, which, however, related to the broader questions of judicial tests employed in review of constitutionality of orders fixing system or company-wide rates for monopolistic or semi-monopolistic enterprises. The specific and controlling issue raised—whether "cost-of-service" evidence is, as a matter of law, required where but one among many of a producer's rates is in issue—was not considered. No reference was made to precedents applicable to such rate proceedings of limited scope, which establish that the line of authority cited by the Court actually has no applicability in such proceedings. The Court concluded by affirming the order and noting approval of a "requirement" for

[7] See *Gulf Oil Corporation, et al.* v. *Federal Power Commission*, 255 F. 2d 556, 557 (5th Cir. 1958).

"cost-of-service" presentations as "reasonable," but without analysis of the Commission's conclusions of law that both the Act and the Constitution, rather than Commission discretion, impose such a "requirement" in proceedings of limited scope under Section 4 of the Act.

REASONS FOR GRANTING THE WRIT

1. The Court of Appeals has erred in affirming a Commission order based solely upon conclusions of law which are in conflict with principles of law established by this Court and lower federal courts as to:

(a) application of the "reasonableness" standard of rate regulation to test a rate which is but one of many of a regulated company's rates (*e.g., Baltimore and O. R. Co.* v. *United States*, 345 U.S. 146 (1953); *Northern Pacific R.R. Co.* v. *Dept. of Public Works*, 268 U.S. 39 (1925); *Illinois Central R. Co.* v. *Interstate Commerce Commission*, 206 U.S. 441 (1907); *Chicago Board of Trade* v. *United States*, 223 F. 2d 348 (D.C. Cir. 1955); *Pan American World Airways, Inc.* v. *Civil Aeronautics Board*, 256 F. 2d 711 (D.C. Cir. 1958), *cert. den.* 358 U.S. 836 (1958)); and

(b) "constitutional requirements" for "cost-of-service" evidence in proceedings limited to the issue of reasonableness of but one of many of a company's rates. (*e.g., Baltimore and O. R. Co.* v. *United States*, 345 U.S. 146 (1953); *Chicago Board of Trade* v. *United States*, 223 F.2d 348 (D.C. Cir. 1955); *RCA Communications* v. *United States*, 43 F. Supp. 851 (S.D.N.Y. 1942)).

By affirming the Commission, the Court of Appeals, in effect, approves imprecise conclusions of law and

decisional inconsistencies as to statutory "requirements", criticized by the United States Court of Appeals for the Fifth Circuit in ten analogous independent producer rate cases remanded to the Commission for further proceedings.[8]

2. The Court of Appeals has erred in failing to review the conclusions of law which were the agency's only decisional grounds, and in affirming the order on grounds advanced for the first time during the process of judicial review. The Court thus violated the principles laid down in *Sunray Mid-Continent Oil Company* v. *Federal Power Commission*, 353 U.S. 944 (1957); and *Securities & Exchange Commission* v. *Chenery Corp.*, 318 U.S. 80 (1943).

3. The decision of the Commission and the opinion of the Court of Appeals raise questions of both legal and economic significance at the inception of federal regulation of prices of natural gas in the fields of production. Section 4(e) of the Natural Gas Act permits various rates to be fixed by separate, individualized contracts for each sale by a producer.[9] Under the

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[8] See *Bel Oil Corporation, et al.* v. *Federal Power Commission*, 255 F. 2d 548 (5th Cir. 1958); *Sun Oil Company* v. *Federal Power Commission*, 255 F. 2d 557 (5th Cir. 1958); *Gulf Oil Corp., et al.* v. *Federal Power Commission*, 255 F. 2d 556 (5th Cir. 1958); *Associated Oil & Gas Co.* v. *Federal Power Commission*, 255 F. 2d 555 (5th Cir. 1958); *Forest Oil Corporation, et al.* v. *Federal Power Commission*, 263 F. 2d 622 (5th Cir. 1959); *H. F. Sears, et al.* v. *Federal Power Commission*, 263 F. 2d 626 (5th Cir. 1959). Compare the Court's references to *Re Pan American Petroleum Corp., et al.* 19 F.P.C. 463 (1958), (decided only ten days prior to Commission decision in the instant *Pan American* case) in the *Bel Oil Corporation* case, and to the Commission's position in the *Forest Oil Corporation* case.

[9] See *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956).

Commission's conclusions of law in the instant case, proceedings under that section, limited to the question of reasonableness of one price in one contract, cannot be decided expeditiously. Instead, these proceedings must be held in abeyance for years while an attempt is made to pinpoint a "cost-of-service" or "revenue requirements" based, of necessity, upon thousands of other sales prices and unrelated business transactions not in issue. Whether this effort is required by the Act and the Constitution, or, alternatively, whether the Commission has the power to decide the issue of reasonableness by reference to other objective types of evidence, is a controlling issue in more than 2,300 independent producer rate proceedings now pending under Section 4(e) of the Act.[10] The holding below has interjected further confusion and uncertainty.

Review by this Court is essential to correct errors of law and to clarify Commission power in rate regulation—an area which is fundamental to the administration of the Natural Gas Act and to the sales activity of the natural gas producing industry.

I. The Court of Appeals and the Commission Have Misconstrued Decisions by This Court and Failed to Follow Precedents Applicable Where But One of Many of a Regulated Company's Rates Is in Issue.

The issues before the Court of Appeals were, we believe, of first impression under the Natural Gas Act. In the development of rate regulation, however, agencies and the courts have considered the specific problems of applying the standard of "reasonableness"

[10] Federal Power Commission Release No. 10,568, G-5562 (PUB), August 12, 1959, states that of 39,398 independent producer rate filings tendered between June 7, 1954, and July 31, 1959, 2,354 price changes were suspended and still pending as of July 31, 1959.

to test a rate for a single sale or "service" which is but a small segment of a regulated company's activities.

Like producers of natural gas, the vast number of businesses now subject to rate regulation, including air carriers, railroads, motor carriers, and crude oil pipelines, characteristically are engaged in a wide variety of activities performed at various rates, many of which are influenced by competitive transportation and market conditions. Other regulatory bodies, unlike the Federal Power Commission in this case, have construed the "reasonableness" standard as permitting a decision where but one rate is in issue by reference to such objective and probative factors as value of service, value of the commodity involved, comparisons with other rates, economic circumstances, and impact of the rate upon an ultimate market.

The courts have considered and recognized the practical and legal foundations for such statutory construction, both of which are highly pertinent in this and other independent producer rate cases under Section 4(e) of the Act: first, it is virtually impossible to determine a separate "cost-of-service" for but one rate of many hundreds of rates; and second, where but one among many rates is in issue, tests of constitutionality of rate orders, measured by rates of return or earnings of a system or a company as a whole, are not applicable.

Both commissions and courts have recognized that the "reasonableness" standard grants this latitude to a regulatory body because ". . . mathematically precise calculations of rates of return and costs cannot be made in respect to minute segments of a huge business . . ." and ". . . to achieve a fair rate of return for a whole

system, composed of many services, the rates on some services must necessarily be above the norm and on other services below it."[11]

These constructions of the "reasonableness" standard are within the framework of the broader, and virtually uniform, holdings that the standard consists of a zone within which an agency is free, as a legislative

[11] *Chicago Board of Trade* v. *United States*, 223 F. 2d 348 (D.C. Cir. 1955). In that case involving the reasonableness standard in the Federal Communications Act, the Court of Appeals briefly referred to the development of this rule of "well-established law." As the Court concluded, the "standard" set for system-wide determinations in *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944), is inapplicable to determination of "a single rate among many rates," which is a "charge for a single service among many services and involves a very small segment of the carrier's business." The Court traced the rule from the Interstate Commerce Commission's construction in 1905 that reasonableness of such a single rate depends upon "'the value, volume and other characteristics affecting the transportation of that particular commodity.'" Recognition of the rule was noted in *Illinois Cen. R. Co.* v. *Interstate Commerce Commission*, 206 U.S. 441 (1907), and in *Northern Pacific R.R. Co.* v. *Dept. of Public Works*, 268 U.S. 39 (1925), and by the Commerce Court in *Lehigh Valley R.* v. *United States*, 204 Fed. 986 (Comm. Ct. 1913). See also *Interstate Commerce Commission* v. *Union Pacific Ry. Co.*, 222 U.S. 541, 549 (1912); *Dayton-Goose Creek R. Co.* v. *United States*, 263 U.S. 456 (1923); *Brundred Bros.* v. *Prairie Pipeline Co., et al.*, 68 I.C.C. 458 (1922); *Pan American World Airways, Inc.* v. *Civil Aeronautics Board*, 256 F. 2d 711 (D.C. Cir. 1958); *Chicago M., St. P. & P. R. Co.* v. *Board of R. R. Comm'rs.*, 255 P. 2d 352 (Sup. Ct. Mont. 1953), and SHINN, REASONABLE FREIGHT RATES, p. 107 (1952). In contrast to this rule, the Federal Power Commission's construction of Section 4(e) of the Natural Gas Act was that reasonableness of a single rate cannot be decided unless the evidence shows whether the rate satisfies the "end result" test in *Federal Power Commission* v. *Hope Natural Gas Co.*, *supra*. But cf. *Re Pan American Petroleum Corp.*, 19 F.P.C. 463 (1958); *Federal Power Commission* v. *Sierra Pacific Power Co.*, 350 U.S. 348 (1956); *Market Street Railway Co.* v. *Railroad Commission*, 324 U.S. 548 (1945).

matter, to find various rates to be just and reasonable.[12] There is no requirement that every rate be at the pinpoint of confiscation—*i.e.*, "the lowest reasonable rate."

The cognate question of whether, as the Commission concluded in this case, there is a constitutional "requirement" for "cost-of-service" studies in all cases was considered in *Baltimore and O. R. Co.* v. *United States*, 345 U.S. 146 (1953), but this Court's holding was not followed by the Court of Appeals below. The Interstate Commerce Commission had fixed maximum rates for but one type of service without reference to "cost-of-service" evidence. In attacking the Commission order in the District Court, the carrier's sole basis for a charge of confiscation was an allegation that the rate prescribed would produce less revenue than alleged "costs" shown by studies proffered in the District Court. This Court enumerated the many factors considered by the Commission relating to value and other circumstances, and held that there was no requirement even for consideration of "cost-of-service" studies, and that the due process clause of the Fifth Amendment cannot be construed as a bar to fixing

[12] The Court of Appeals below merely assumed the existence of this zone of reasonableness, although it has been recognized by the Courts for more than half a century. As stated by Mr. Justice Cardozo in *United States* v. *Chicago, M., St. P. & P. R. Co.*, 294 U.S. 499, 506 (1935): "There is no suggestion in the report that the rates have been so reduced as to be less than compensatory. True they do not reach the maxima beyond which charges are excessive. On the other hand, they do not pass the minima beyond which charges are too low. A zone of reasonableness exists between maxima and minima within which a carrier is ordinarily free to adjust its charges for itself." See also *Montana Dakota Utilities Co.* v. *Northwestern Public Service Co.*, 341 U.S. 246, 251 (1951); *Denver Union Stockyard Co.* v. *United States*, 304 U.S. 470 (1938); *Banton* v. *Belt Line Ry. Corp.*, 268 U.S. 413 (1925); *Simpson* v. *Shepard*, 230 U.S. 352 (1913).

rates without reference to "cost-of-service" for a single service.[13]

Similarly, the issue in this case under Section 4(e) of the Act was limited to reasonableness of a price for a sale which is but one of hundreds of sales by Pan American subject to the Commission's jurisdiction. For each of the other owners, whose sales are covered by the single rate schedule under Commission regulations, the price in issue is for a sale which is also but one of their many business transactions, including hundreds of other sales of natural gas in various other fields, many of which are subject to Commission regulation. The substantial question of whether there would be no constitutional or statutory requirement for "cost-of-service" evidence if all of the regulated sales prices of a producer were in issue, was not before the Commission or the Court of Appeals, and is not before this Court. *Cf. Market Street Railway Co.* v. *Railroad Commission*, 324 U.S. 548 (1945). However, as to the one price in issue, it is obvious that determining a so-called "cost-of-service" would require the attempted isolation of a "cost" for the one sale from the total costs and revenues of the en-

[13] Among the factors were value of the commodity, comparison of commodity values, comparison of rates on the same commodities, comparisons with other rates on other commodities, special characteristics of the service, competing rates, and the possible effect of rates upon prices in ultimate markets (345 U.S. at 149-150). This Court's opinion recognizes that neither the "just compensation" nor "due process" clauses impose such an inflexible "requirement" (345 U.S. at 148). See also *Railway Express Agency* v. *United States*, 6 F. Supp. 249, 253 (S.D.N.Y. 1934), and cases cited in fn. 11, *supra*, reviewing rate determinations under federal regulatory statutes.

tire business activities of each of the many producer-sellers.[14]

Despite this, the Court of Appeals apparently failed to recognize that the Commission reached specific conclusions as to statutory and constitutional "requirements" for "cost-of-service" evidence. It was clear on the face of the order under review that the Commission had construed Section 4(e) of the Act as universally restricting its power to act unless "cost-of-service" studies are presented. Equally clear was the Commission's conclusion that, contrary to the principles applicable where but one among many rates is in issue, it could decide the case only by application of the "end result," or *Hope* test, and that a decision without reference to "cost-of-service" studies or "revenue requirements" of the producers' whole operations, would be proscribed by the Fifth Amendment.

The validity of these Commission conclusions was raised in the petition for review, the briefs and in oral argument, but these controlling issues were not considered below. The Court referred only to inapplicable general criteria employed at times by the judiciary when constitutionality of an order prescribing a whole body of rates has been in issue. Precedents applicable to a rate proceeding of limited scope, such as under Section 4(e), were not considered. In view of the controlling issues raised by the Commission's order and the number of producers involved, the Court of Appeals' references to a showing by "petitioners," in the plural, as to "its" operations, in the singular, and, again to the needs of the "gas companies," in

[14] Cf. Re *Pan American Petroleum Corporation, et al.*, 19 F.P.C. 463 (1958).

the plural, and "its" costs, in the singular, engender further uncertainty, rather than clarify the requirements to be met under Section 4(e) of the Act.

The Commission's conclusions as to limitations upon its powers in proceedings under Section 4(e) were patently erroneous, and the Court of Appeals has erred in not reversing the Commission. Unless this Court corrects these constructions of the Act and conclusions of law as to constitutional "requirements" in proceedings of limited scope, both independent producers and the Commission will remain enmeshed in disorder which has already prevailed for more than five years.

II. The Court of Appeals Deprived Petitioner of the Substance of Judicial Review by Failing to Consider the Questions Raised by the Commission's Decision, and by Affirming the Commission's Order Upon Grounds Advanced for the First Time Before the Court.

The question before the Court of Appeals for adjudication was whether the Commission's constructions of the statute and the Constitution were correct. In clear and unmistakeable language, the Commission had held, as a matter of law, that conventional "cost-of-service" evidence is a statutory and constitutional prerequisite to the exercise of its discretion to decide upon reasonableness of a rate, and that it was required to deny the producers' instant rights to the price in issue solely because of the absence from the record of such "cost-of-service" evidence.

Nevertheless, in the Court of Appeals, the position taken by the Commission's brief was that the Commission, in its discretion, had found such evidence to be necessary to justify a price increase. The order thus was not defended upon the grounds upon which it was actually predicated. Instead, it was argued

that had the Commission correctly construed the scope of its discretion, in exercising that discretion it could have reached the same conclusion, and that, as a consequence, the order should be held valid as an exercise of discretion.

During the briefing process, the Commission's departure from its decisional grounds, and virtual abandonment of the conclusions below, was called to the attention of the Court of Appeals. Despite this, the Court of Appeals ignored the controlling issues clearly raised by the Commission's holding, and substituted as the issue before it, the question of whether the "evidence is sufficient to compel" reversal of the Commission order. Proceeding from this substitution, the Court then affirmed, ostensibly as a "reasonable" requirement by the Commission in its discretion what the Commission itself had actually held as a matter of law to be requirements imposed by the statute and the Constitution.[15]

The Court of Appeals thus deprived the petitioners of the substance of judicial review. An administrative order was based upon constructions of the statute and the Constitution; on review, petitioners challenged the validity of the order on the grounds that these conclusions, which were the exclusive basis for the order, were erroneous. Under the review procedure, if the Court found the Commission's conclusions of law to be incorrect, the Court's duty was to lay bare the error of law and remand the case for further consideration of the evidence by the Commission. Whether an identical order of denial of the increase as unjustified by

[15] Compare the statement of the "central issue" and decisional grounds in the Commission's orders, *supra*, p. 9, with the statement of the question by the Court of Appeals, *supra*, p. 12.

the evidence would have been valid, *if* the Commission had reached that conclusion as an ultimate finding of fact in exercising its discretion, was not the question before the Court. The Commission had concluded that a legal condition precedent was unsatisfied, and the evidence in the case had never been weighed in terms of administrative discretion.[16]

Unquestionably, under the decisions of this Court, petitioners are entitled to independent judicial review of conclusions of law which are an agency's decisional grounds.[17] Section 19(b) of the Natural Gas Act and

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[16] Before the Commission, Pan American explicitly requested the Commission, by findings and conclusions, to make clear what its decision as to reasonableness of the price, upon the evidence presented, would have been, had the Commission not held that, as a matter of law, "cost-of-service" was required. Just as explicitly, the Commission held that such findings and conclusions were "of no moment," since "under the law," "cost-of-service" evidence was required. (R. 3498-3499).

[17] As stated in *Stark* v. *Wickard*, 321 U.S. 288, 310 (1944), the courts, under Article III, are established "to adjudicate cases and controversies as to claims of infringement of individual rights whether by unlawful action of private persons or by the exertion of unauthorized administrative power." When the Federal Power Commission, existing under Article I, deprives individuals of vested contract rights, judicial review must be accorded those aggrieved thereby. *Cf. Keller* v. *Potomac Electric Power Co.*, 261 U.S. 428 (1923). Legislative history of the Administrative Procedure Act clearly discloses the intention of Congress to preserve independent review of actions of such agencies, despite the vast administrative powers delegated. Under Section 10(e), "[r]eviewing courts are required to decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of any agency action. • • • This section provides that questions of law are for courts rather than agencies to decide in the last analysis and it also lists the several categories of questions of law." Administrative Procedure Act, Legislative History, Sen. Doc. No. 248, 79th Cong. 2d Session, 278 (1946):

Section 10(e) of the Administrative Procedure Act establish procedural avenues, but, as this case exemplifies, whether the substance of judicial review is actually accorded, must, in the last analysis, depend upon whether the Courts of Appeals follow the precepts of review this Court has laid down in many contexts.

Well-defined are the rules of court-agency relationships that it is a judicial function to decide the limits of statutory power,[18] and that if an agency decides a matter upon conclusions of law, its decision must stand or fall upon the legal validity of those conclusions.[19] Applying these rules in specific cases, this Court has prohibited affirmance of agency orders upon substituted decisional grounds, and, under the Natural Gas Act, has struck down, regardless of the subtleties employed, substitution of questions and decisional grounds by parties or by the Court of Appeals, *sua sponte*, during the course of judicial review.[20] Only two years ago,

[18] Aside from the "law-fact" distinctions, it is settled that even when it construes a statute, an agency is still acting "legislatively," and the statutory construction ultimately is a judicial function. See *Social Security Board* v. *Nierotko*, 327 U.S. 358 (1946); *Addison* v. *Holly Hill Fruit Products*, 322 U.S. 607 (1944), *reh. den.* 323 U.S. 809 (1944); *United States* v. *Rosenblum Truck Lines*, 315 U.S. 50 (1942); *Stark* v. *Wickard*, 321 U.S. 288 (1944).

[19] *Securities & Exchange Commission* v. *Chenery Corp.*, 318 U.S. 80 (1943).

[20] *Federal Power Commission* v. *Colorado Interstate Gas Co.*, 348 U.S. 492 (1955). Other cases have emphasized that the judicial function does not extend to approval of Federal Power Commission action upon grounds not clearly stated in the Commission's orders. See *Connecticut Light & Power Co.* v. *Federal Power Commission*, 324 U.S. 515 (1945); *Federal Power Commission* v. *Idaho Power Co.*, 344 U.S. 17 (1952) *reh. den.* 344 U.S. 910 (1952); *Federal Power Commission* v. *Pacific Power & L. Co.*, 307 U.S. 156 (1939).

this Court held that a court exhausts its powers under Section 19(b) of the Act when it finds Commission construction of the statute to be erroneous, and that it is error for a court to proceed further and affirm the Commission upon other grounds. *Sunray Mid-Continent Oil Company* v. *Federal Power Commission*, 353 U.S. 944 (1957).

The Court of Appeals below has violated these directives, and petitioner here and the persons it must represent thus have been subjected to what apparently has become a four-step pattern in independent producer rate cases and to which the Court of Appeals for the Fifth Circuit has already obliquely referred.[21] First, an order is based upon broadly stated constructions of the Act and the Constitution and conclusions of law that the Commission has no discretion to act;[22] second, this order is not defended in the Court of Appeals upon the stated decisional grounds, but upon the entirely different ground that there has been a proper exercise of discretion on particular facts; third, a Court of Appeals, without analysis of the stated conclusions of law but also without clearly stating its grounds, affirms the order, apparently as a proper exercise of administrative discretion upon the evidence in the case; fourth, the Court's opinion is thereafter cited as specifically affirming the agency's original, broad statutory constructions and conclusions of law that no discretion exists.[23]

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[21] Compare *Bel Oil Corporation* v. *Federal Power Commission*, 235 F. 2d 548 (5th Cir. 1958) and *Forest Oil Corporation* v. *Federal Power Commission*, 263 F. 2d 622 (5th Cir. 1959).

[22] See decisional grounds, *supra*, pp. 9-10.

[23] For example, within four days after the issuance of the Court's opinion in this case, that opinion was cited not as affirming discretion of the Commission to require and consider either "cost-of-

All four steps in this pattern have already been applied in this case and will continue to be applied unless this Court directs the federal courts to accord to petitioner and others similarly situated, the full, independent judicial review of agency conclusions of law required by Section 19(b) of the Act. Under administrative practice, the legislative policy and functions to which the Commission and its Staff must be committed, under the statute, are such that no presumption of absolute objectivity can reasonably attach to their opinions upon questions of law. Since private rights, on the one hand, and this legislative policy, on the other, always are affected by the legal questions, it is only upon review under Section 19(b) that a judicial weighing of the issues generally or logically is expected. If, during the review procedure, conclusions of law by the administrative agency are not reviewed, there is no step in the regulatory procedure which satisfies requirements of substantive or procedural due process of law.

Thus, in this and other cases, the question of whether the Commission is right or wrong in holding, as a matter of law, that the Act and the Constitution prohibit a decision by it unless "cost-of-service" evidence is presented in proceedings under Section 4(e), is by its nature a question for the Courts of Appeals to decide. If, as occurred below, a reviewing court permits

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service" or other forms of evidence, but for the proposition that ". . . until such time as the present statute is amended to permit such use [of other types of evidence], it is respectfully submitted that the rates of natural-gas companies for sales of gas in interstate commerce for resale must be fixed and determined under the conventional cost-of-service method of rate-making." Brief of Commission Staff Counsel, In the Matter of Alfred C. Glassell, Jr., individually and as co-trustee for Alfred Glassell Comegys Trust, *et al.*, FPC Docket No. G-9278, pp. 42-43 (June 22, 1959).

alteration of decisional grounds, the procedural avenues of Section 19(b), and of Section 10(e) of the Administrative Procedure Act, become mere form, and there is no judicial review of agency conclusions of law.

The holding below is based upon such an alteration and a substitution of decisional grounds by the Court. The Court erred in failing to consider the issues raised by the original decisional grounds set forth in the Commission's order, or, since the Commission abandoned its original grounds, in failing to remand the case for further proceedings before the Commission. *Sunray Mid-Continent Oil Company* v. *Federal Power Commission*, *supra*; *Federal Power Commission* v. *Idaho Power Co.*, 344 U.S. 17 (1952); *Connecticut Light & Power Co.* v. *Federal Power Commission*, 324 U.S. 515 (1945).

III. The Questions are of Utmost Importance in Regulation of the Gas Producing Industry Under the Natural Gas Act and Should be Resolved Promptly.

This Court held in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 332 (1956), that Section 4(e) recognizes that separate, individualized contracts are required by operating conditions and the competitive nature of the natural gas industry. Approximately 10,000 such contracts between producers and pipeline companies have already been filed with the Commission as separate "rate schedules."[24]

[24] FPC Release No. 10,568, G-5562 (PUB), August 12, 1959, reports that between the date of the *Phillips* decision and July 31, 1959, producers had filed 14,770 applications for certificates covering sales. Under the regulations governing producer filings, the sales contract is filed as a rate schedule at the time application is made for a certificate, or prior to commencement of deliveries.

Almost without exception, each of these contracts, or "rate schedules," contains one or more provisions customary in the industry for agreed-upon changes in prices at varying times, in varying amounts, and for varying reasons. Under Commission regulations notice of each such change of price under each contract must be filed as a separate "change" of the "rate schedule," and each such change of price is thus subject to suspension and separate hearing upon reasonableness under Section 4(e). As of July 31, 1959, the Commission reported that there were pending 2,354 suspension cases under Section 4(e) involving price changes by producers.[25]

In each such proceeding the question arises whether, as a matter of law, a so-called "conventional" company-wide "cost-of-service" presentation is required before reasonableness of the one price in issue may be determined, or whether, in Commission discretion, reasonableness of the specific price in question may be determined by more expeditious means available to the Commission and without recourse to the "cost-of-service" formulae.

Numerous and complex regulatory problems before the Commission and the gas producing industry in these producer rate cases arise from the insurmountable difficulty of attempting to apply these formulae to each of thousands of independent producers, and to each of their separate sales and prices. Producers simply are not classic utilities and cannot be fitted into the mold. As the record in this case demonstrates, the producing industry is characterized by multiple ownership of interests in individual leases, and of gas de-

[25] *Ibid.*

livered under the terms and prices in any one contract; by a vast diversity of activities by the owners of production; by arm's-length negotiation of the separate prices for each sale; by the joint production of gas with other commodities not subject to Commission regulation; by a lack of relationship between cost incurrence and sales prices controlled by a competitive market; and, by the practical impossibility of bestowing upon producers' exploration, production, and sales activity, the franchises or other protective devices characteristic of companies to which the "cost-of-service" technique has been applied in the past.

After the *Phillips* decision in 1954, both the gas producing industry and the Commission had anticipated the necessary adaptation of methods of rate regulation to these technical and economic characteristics of the producing industry, as has occurred when other industries first became subject to federal regulation. Unfortunately, such adaptation is now virtually precluded by judicial decisions such as that by the Court below, which are interpreted as limiting the Commission's powers.

The impact of these decisions upon the administration of the Act and upon the producing industry has been a virtual halt of the rate review process. Under the holdings below, each of the many hundreds of pending, limited proceedings under Section 4(e) must become a process of years' duration, while each of hundreds of producers and the Commission's staff attempt to devise a company-wide "cost-of-service" presentation in forms used in proceedings relating to totally dissimilar operations of pipeline companies. In addition, because of interrelations of prices in the fields, pipeline companies' rates, and the rates of com-

panies distributing natural gas to local consumers, prices all the way from the producing fields to the points of consumption in distant states are thus rendered uncertain.

Resolution of the questions of legal limitations upon the Commission's power is, therefore, essential if the Commission is to exercise, with any expedition, the jurisdiction recognized in the *Phillips* decision. If the Commission is to use latitude in rate review under Section 4(e), and may, as have other agencies, adapt the process of regulation to the specific and unchangeable characteristics of the industry regulated, clarification by this Court of the scope of Commission powers is necessary.

Resolution of the second question is of equal importance. Increasingly, in its rate proceedings, the Commission has found it necessary to dispose of questions of statutory construction in applying the Act to the previously unregulated producing industry, and, since the *Mobile* decision, to decide initially questions of contract interpretation and other legal issues. Statutory procedures require the Courts to review, independently, such constructions, constitutional interpretations, and conclusions of law by administrative bodies, where these determinations are challenged. By restriction of inquiry and failure to pass upon such controlling issues of law, reviewing courts cannot exercise their exclusive review jurisdiction, and the substance of due process disappears from review procedures. However, even if the conclusions of law have been made by the Commission during the course of rate review under Section 4(e), adherence by a reviewing court to principles laid down in such cases as *Securities & Exchange Commission* v. *Chenery Corp.*,

supra, must be required. Recent cases under Section 19(b) of the Act, involving independent producers, have been marked by departures from those principles, but none of the objectives of regulatory statutes can warrant this erosion of the bounds of judicial and agency functions so carefully preserved by this Court.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that this Petition for Writ of Certiorari should be granted.

W. W. HEARD
JOHN F. JONES
Pan American Petroleum Corporation
P. O. Box 591
Tulsa 2, Oklahoma

WILLIAM J. GROVE
CARROLL L. GILLIAM
Dow, Lohnes and Albertson
600 Munsey Building
Washington 4, D. C.

Attorneys for Petitioner

September, 1959

APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 14581

EPISCOPAL THEOLOGICAL SEMINARY OF THE SOUTHWEST, ET AL., *Petitioners*,

v.

FEDERAL POWER COMMISSION, *Respondent*.

No. 14588

CONTINENTAL OIL COMPANY, *Petitioner*,

v.

FEDERAL POWER COMMISSION, *Respondent*.

On Consolidated Petition for Review of Orders of the Federal Power Commission, and on Motion of Respondent in No. 14581 to Dismiss Petition for Review.

Decided June 18, 1959

Mr. John F. Jones of the Bar of the Supreme Court of Oklahoma, *pro hac vice*, by special leave of court, and *Mr. William J. Grove* with whom *Mr. Carrol L. Gilliam* was on the brief for petitioners. *Mr. Roland B. Voight* also entered an appearance for petitioner in No. 14588.

Mr. Howard E. Wahrenbrock, Solicitor, Federal Power Commission, with whom *Messrs. Willard W. Gatchell*, General Counsel, Federal Power Commission, *W. Russell Gorman*, Assistant General Counsel, Federal Power Commission, and *Robert M. Weston*, Attorney, Federal Power Commission, were on the brief for respondent.

Before Mr. Justice REED, retired,* and PRETTYMAN, Chief Judge, and FAHY, Circuit Judge.

* Sitting by designation pursuant to the provisions of Sec. 294 (a), Title 28, U. S. Code.

REED, Associate Justice: This is an appeal by more than some seventy independent producers of natural gas all of whose properties are in the Woodland gas field, Harrison County, Texas, from two orders of the Federal Power Commission. One producer, Stanolind Oil and Gas Company, is not only a producer, i.e., owns certain gas producing land or rights in the field, but also is an operator, i.e., one who sold under a twenty-year contract and regularly delivered its own gas and that of other producers involved to the Mississippi River Fuel Corporation for handling and transmission in interstate commerce. One nonoperating owner, Continental Oil Company, joined with Stanolind in the sales contract.

This contract, entered into April 3, 1951, contains a price escalation clause which calls for gradual raises of the price at two, three or four year intervals from twelve to fifteen and a half cents for each one thousand cubic feet. After the decision of the Supreme Court of the United States in the *Phillips Petroleum* case on June 7, 1954,[1] which held that sales and deliveries within the producing state by producers and their intermediaries for resale by distributing companies are in interstate commerce, regulable by the Federal Government and covered by § 4 of the Natural Gas Act, Stanolind Oil and Gas Company, now known in this record, after a change of name, as Pan American Petroleum Corporation, filed the sales contract between themselves and Mississippi River Fuel Corporation with the Federal Power Commission.

The contract was filed October 18, 1954, as Stanolind's Gas Rate Schedule No. 31, pursuant to an order of the Commission of July 16, 1954, requiring independent producers to file as rate schedules all contracts for sale of their gas covered by the Act under the *Phillips* decision.[2]

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[1] Phillips Petroleum Corp. v. Wisconsin, 347 U. S. 672.

[2] Continental Oil Co. likewise filed the contract as its Schedule No. 107. Proceedings in that case followed the same course as those of Pan American and need not be detailed.

The Regulations of the Commission required the filing of a copy of the contract and a showing of the service provided and the rates and charges.[3] These were the rate schedules. Regulatory provision was made for changes in the rate schedules. The applicable sections appear below.[4] The contract was received and accepted by the Commission pursuant to Regulation 154.101.[5]

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[3] Regulations under Natural Gas Act, §§ 154.91-154.102.

[4] § 154.93. Rate Schedule Defined

"For the purpose of Sections 154.92 through 154.101 hereof 'Rate Schedule' shall mean the basic contract and all supplements or agreements amendatory thereof, effective and applicable on and after June 7, 1954, showing the service to be provided, and the rates and charges, terms, conditions, classifications, practices, rules and regulations affecting or relating to such rates or charges, applicable to the transportation of natural gas in interstate commerce or the sale of natural gas in interstate commerce for resale subject to the jurisdiction of the Commission."

§ 154.94 Changes in Rate Schedules

"(a) No change shall be made in any rate, charge, or service in effect on and after June 7, 1954, for the interstate transportation or sale of natural gas in interstate commerce subject to the jurisdiction of the Commission by any independent producer required to file rate schedules pursuant to Section 154.92 hereof, without first filing a change in rates pursuant to Section 4(d) of the Natural Gas Act and in accordance with this section.

. . . . . .

"(e) The operation of any provision of the rate schedule providing for future or periodic changes in the rate, charge, classification, or service after June 7, 1954, or the operation of any like provision in any initial rate schedule filed after June 7, 1954, shall constitute a change in rate schedule."

[5] § 154.101 Acceptance for filing not approval.

"Acceptance for filing of any rate schedule or part thereof, or of a Notice of Cancellation or Termination, is not to be construed as approval by the Commission, nor to serve in lieu of any requirements under Section 7 of the Natural Gas Act."

The incident that brought on this litigation was a filing on March 2, 1955, of a notice of a change in the rate schedule. This was done in involuntary compliance with sections 154.94 (a) and (c) of the Regulations just referred to. It proposed a raise from 13 cents to 13.5 cents per mcf, in accordance with the provisions of the contract's escalation clause. The filing was done under protest and with reservation of a right to object. The Commission suspended the change under section 4 of the Natural Gas Act, particularly subsection (e).[6] This was the first order challenged. A consolidated hearing was

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[6] 15 U.S.C. § 717c (e):

"Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, or State commission, or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; . . . At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible."

Pan American Petroleum Corp., 19 F.P.C. 519, 525:

"On September 29, 1955 the Commission issued an order making Supplement No. 8 to Continental's F.P.C. Rate Schedule No. 107 effective as of September 3, 1955 subject, however, to refund under bond of such portion of the increase as might be found not justified. A similar order was issued with respect to Supplement No. 10 of Stanolind's F.P.C. Rate Schedule No. 31 on October 24, 1955. Thus that rate Schedule also became effective on September 3, 1955 subject to an undertaking by Stanolind to refund any part of such increase found to be unreasonable and unlawful."

held thereafter on the reasonableness of the changes of rate filings of Pan American and Continental. The decision therein was the second order challenged. The Commission found against petitioners on both orders, approving so far as is here material the Examiner's prior decision.[7]

The Examiner and the Commission held that the contract, including the escalation clauses, filed in accordance with 15 U.S.C. § 717g (c)[8] was subject to the hearing as ordered by the Commission under 15 U.S.C. § 717c (e), set out in note 6, supra, on the attempted use of the escalation clause by the operator, Pan American Petroleum Corporation, to increase its rate.[9] In adopting the Examiner's decision, the Commission said:

[7] The F.P.C. decision of April 14, 1958, and the Presiding Examiner's decision of February 8, 1957, appear in 19 F.P.C. 519 and 523.

[8] 15 U.S.C. § 717c (c):

"Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from June 21, 1938) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services."

[9] The Examiner said:

"It seems clear that to accept the contention of the Applicants that 131e is an initial rate not subject to the provision of suspension and the other provisions of Section 4 of the Act would virtually nullify those provisions. To permit the terms of an initial contract (or rate schedule) to govern permanently the future rates to be charged thereunder insofar as Section 4 is concerned would leave the Commission powerless to exercise its functions under that section. To escape entirely its responsibilities under Section 4 and avoid the necessity of establishing the fairness and reasonableness of future increases in rates as contemplated therein, a natural-gas company would need only to include in the initial contract provision for all remotely conceivable future increases." 19 F.P.C. at 534.

"It is sufficiently apparent by now that, both as a matter of law and Commission regulatory policy, every change of an existing rate to a different price by reason of a step-up escalation clause in a sales contract constitutes a change in rate, and every such change is subject to suspension by virtue of Section 4 (e) of the Act. See, e.g., *Mississippi River Fuel Corporation*, 2 F.P.C. 170, 176; aff'd, *Mississippi River Fuel Corp.* v. *Federal Power Commission*, 121 F. 2d 159; Section 154.94 (c) of F.P.C. Regulations under the Natural Gas Act." 19 F.P.C. at 521.

It was determined also that the companies had not carried their burden of showing under § 4 (e) of the Natural Gas Act, 15 U.S.C. § 717c (e), note 6, supra, that the increases sought were just and reasonable.[10]

Rehearing of the Commission's orders suspending and denying the requested increase was requested by an appropriate application pursuant to § 19 of the Natural Gas Act.[11] It was denied June 6, 1958, —— F.P.C. ——.

Petitioners' objections drawn from their Statement of Points are basically two:

"I. The suspension order is invalid; the Commission had no jurisdiction or authority to proceed under Section 4 of the Natural Gas Act because the 13.5¢ contract price is not a 'change' of 'rate schedule.'

"II. The Commission erred in concluding that Petitioners failed to sustain the burden of proving the contract price just and reasonable, and, in 'disallowing' receipt of the contract price."

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[10] 19 F.P.C. at 521 and 538.

[11] 15 U.S.C. § 717r (a).

Other points were made which really fall within those main points.

> "III. The Commission unlawfully modified Petitioners' contract without having made, as required by Section 5 of the Act, an express finding that the price is unreasonable."

This turns upon the same issue as Point I in the above text. If the Commission may deal with the petitioners' notice of a change in the rate schedule under Section 4 of the Act, note 6, supra, petitioners' objection that Section 5, in so far as it requires a finding by the Commission that the rate is unreasonable, was disregarded by the Commission, falls.[12]

> "IV. The Commission failed to make basic and ultimate findings of fact and conclusions as required by substantial evidence with the result that the Commission acted arbitrarily, abused its discretion, and violated Section 8 (b) of the Administrative Procedure Act of 1946, 60 Stat. 242, 5 U.S.C.A. § 1007 (b)."

This point seems to be subsidiary to and controlled by petitioners' Point II in the text. Petitioners argue that their evidence as to reasonableness of the price produced by the escalation clause required a finding of its reasonableness. It is charged the Commission ignored this evidence in reaching its conclusion that petitioners had failed to carry the required burden of proof under § 4 of the Act to show the rate increase by the escalation clause was reasonable.[13] This it is argued violated Section 8(b) of the Administrative Procedure Act.[14] That subsection assures an opportunity to litigants to submit to the offi-

[12] See 15 U.S.C. § 717d.

[13] See note 6, supra.

[14] 5 U.S.C. § 1007 (b).

cers of an agency proposed findings, exceptions and reasons therefor. The petitioners presented their petition for rehearing to the Commission and have failed to point out any alleged violations of § 8(b) of the Administrative Procedure Act other than that the Commission ignored "much of this evidence." We think our consideration of petitioners' Point II disposes also of this exception.

First. We turn then to petitioners' Point I that Section 4 of the Natural Gas Act is inapplicable because notice that the escalation clause of the contract would be used to increase its gas rates is not a change of rate schedule under section 4 (d) of the Act.[15] The petitioners assert: "As *filed* with the Commission in October, 1954, and *made effective* as a rate schedule, Petitioners' contract provided for the mutually agreed-upon price of 13.5¢ on April 3, 1955." That is correct. But up to March 2, 1955, the rate fixed by the rate schedule was 13¢.

Regulations by the Commission regarding rate schedules and changes therein were authorized by the Natural Gas Act, Sec. 4 (c).[16] Under that authority the Commission made the regulations set out in note 4, supra, forbidding changes without filing a change in rates and specifically declaring in regulation 154.94 (c) that operation of any future change in rate, such as the escalation clause here involved, shall constitute a change in rate

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[15] 15 U.S.C. § 717c (d):

"Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. . . ."

[16] 15 U.S.C. § 717c (c), see note 8, supra.

schedule. Faced by this regulation, petitioners attack its validity on the ground that section 4 of the Act contemplates "physical replacement" of the old schedule. Administrative bodies can be authorized to pass regulations to enforce the provisions of acts such as the Natural Gas Act "within the permissible bounds of administrative construction."[17] We think this regulation is of that type and valid. The definition of "rate schedule," as stated by Regulation § 154.93, note 4, supra, upon which petitioners rely, was adopted by the Commission. If the Commission had power to adopt that regulation, it had the power to adopt the succeeding regulation, § 154.94 (c), note 4, supra, making the operation of an escalation clause a change in rates.

Furthermore, section 4, subsection (c) of the Act, note 8, supra, requires "schedules showing all rates and charges for any transportation." That must mean the then applicable rate. Section 4 (d), see note 15, supra, requires that the public must be kept informed of the "changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect." No change may be made in a "rate" or "schedule then in force," without notice to the Commission and the public. This language is persuasive that forehanded contractual provisions cannot modify the regulatory provisions of the Act as urged by petitioners. The purpose is to advise the public of a change in the current rate. Petitioners' interpretation would run counter to the language and purpose of Congress to maintain the "lowest reasonable rates."[18] To approve escalation clauses in long term contracts when the contracts were originally filed, would determine rates for indefinite future periods. Fair adjustments of escalation-clause rates to

[17] Morrissey v. Commissioner, 296 U. S. 344, 354-355; cf. United States v. Howard, 352 U. S. 212.

[18] Sec. 5 (a) of the Act.

future costs and earnings would be impossible at that time. Public utility rates cannot be fixed solely by bargaining between producers and distributors. The governmental agency also has the duty to protect the consumer.

But petitioners say that the Supreme Court's decision in *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U. S. 332, rules the question as to whether the actuation of the escalation clause is a change of rate or schedule under § 4 of the Act. They read the case as authority for saying, in petitioners' words, "where a change of price *is not* a change *to* the contract under contract law, then such events likewise are *not* 'changes' of a filed contract or rate schedule or a 'new schedule' under Section 4(d) of the Act, and notice is not required and may not be filed."

Petitioners' deduction from the *Mobile* case, we think, is not applicable to a contract providing for the use of an escalation clause. The issue in the case was whether a natural gas company furnishing gas to a distributing company could unilaterally change a long-term contract rate by filing a new rate schedule with the Commission. Page 333. The Commission's basic power is to regulate any rate it determines is "unjust, unreasonable, unduly discriminatory, or preferential." Page 341. This left the regulated company free, subject to § 4 of the Act and action of the Commission thereunder, to change any rate it had the power, vis-a-vis the distributor, to change (page 342), but the Court held the company had no power by virtue of general law unilaterally to so change its contract without the consent of the distributor. Page 342.[19]

In the *Memphis* case, note 19, supra, the agreement between buyer and seller of gas contained this clause:

"All gas delivered hereunder shall be paid for by Buyer under Seller's Rate Schedule [the appropriate

[19] See United Gas Pipe Line Co. v. Memphis Light, Gas and Water Div., 358 U. S. 103.

> rate schedule designation is inserted here], *or any effective superseding rate schedules*, on file with the Federal Power Commission." (Italics supplied.) P. 105.

There was no sliding scale of rates.[20] The Court of Appeals held that new rates under this long-term contract must be negotiated with and agreed to by the buyer before the new rates can be filed and reviewed under the Act, § 4 (d) and (e). The Supreme Court reversed. It pointed out that *Memphis* differed from *Mobile* in that *Memphis* had a fixed rate but "effective superseding" rates also. It quoted its holding in *Mobile:*

> ". . . except as specifically limited by the Act, the rate-making powers of natural gas companies were to be no different from those they would possess in the absence of the Act: to establish *ex parte*, and change at will, the rates offered to prospective customers; or to fix by contract, and change only by mutual agreement, the rate agreed upon with a particular customer. No more is necessary to give full meaning to all the provisions of the Act: consistent with this, § 4 (d) means simply that *no* change—neither a unilateral change to an *ex parte* rate nor an agreed-upon change to a contract—can be made by a natural gas company without the proper notice to the Commission. . . ." 358 U. S., at 110-111.

and added:

> "Section 4 (d) provides for the giving of notice of any change 'in any such rate . . . or contract relating thereto . . .' by filing new rate schedules with the Commission and keeping them open for public inspection. And § 4 (e) authorizes Commission review of the lawfulness of any such changed rate. The record before us affirmatively shows that United in the filings here at issue has complied with all the duties which these sections in terms impose upon it,

[20] Memphis Light, Gas and Water Div. Federal Power Commn., 250 F. 2d 402, 404; 358 U. S., at 109.

and there is nothing in these sections which even remotely implies that § 4 (d) and (e) procedures are applicable to the filing and review of only those rate changes whose amount has been agreed upon by the seller and buyer." Id., at 111-112.

It was then concluded:

"*Mobile* makes it plain that '§ 4 (d) on its face indicates no more than that *otherwise valid* changes cannot be put into effect without giving the required notice to the Commission.' 350 U. S., at 339-340. (Italics supplied.) The necessary corollary of this proposition is that changes which in fact are 'otherwise valid' in the light of the relationship between the parties can be put into effect under § 4 (d) by a seller through giving the required notice to the Commission. *Mobile* expressly notes that in the absence of any contractual relationship rates determined *ex parte* by the seller may be filed under § 4 (d). 350 U. S., at 343." Id., at 112.

These cases leave the controlling issue here whether there was a change in the rate.

As we indicated above in considering the regulations, we think there was a change in rate. It was an agreed-upon change, it is true. And although the original schedule had foretold the coming of the change, it took an amendment to advise the public and the Commission that the new rate was going into operation. We see nothing in the *Mobile* or *Memphis* cases that hold otherwise. Cf. *Sun Oil Co.* v. *Federal Power Commn.*, —— F. 2d —— (C. A. 5, decided April 17, 1959), slip opinion p. 5; *Kerr-McGee Oil Industries* v. *Federal Power Commn.*, 260 F. 2d 602.

Second. Point II of petitioners' objections to the Commission's order deals with the Commission's determination that petitioners failed to sustain their burden under § 4 (e) of the Act to show the proposed new rate is just

and reasonable.[21] The petitioners argue that the "just and reasonable" rate required to be proven by petitioners under § 4 of the Act may be established by different proof than "the lowest reasonable rates" under § 5.[22] The words "just and reasonable," as applied to limitation of rates, appear both in § 4 and § 5. They are used in § 5 as a guide to the determination of rates.[23] But we need not decide whether there is a difference in proof required between the "just and reasonable" and "lowest reasonable." Since we hold that § 4 is applicable, the Commission's decision may be tested under "just and reasonable," and we may also assume that, as petitioners urge, there may be a zone of reasonableness inherent in such a test. That is, the Commission could consider as just and reasonable various rates within the zone. Such choices are not at issue here. The question in the second point is whether the petitioners' evidence is sufficient to compel us to reverse the Commission's conclusion that the evidence was not enough to sustain the proposed increase.[24]

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[21] See note 6, supra.

[22] Under § 5 the Commission, after hearing, "may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates."

[23] See Federal Power Commn. v. Natural Gas Pipeline Co., 315 U. S. 575, 581-582.

[24] "Likewise, the exceptions of Pan American and Continental to the presiding examiner's determination that the companies had failed to sustain their burden of showing that the proposed increased rates are just and reasonable under our opinion in *Matter of Union Oil Company of California, et al.*, 16 F.P.C. 100, and the court's decision in *City of Detroit* v. *Federal Power Commission*, 230 F. 2d 810, raise no material point not sufficiently dealt with in the presiding examiner's decision. We conclude that the companies have not shown their proposed increased rates are justified, nor can they until they meet the requirements of these decisions." 19 F.P.C., at 521.

As the Examiner pointed out in his decision, 19 F.P.C. 523, "[i]t is beyond dispute that the terms of the agreement were arrived at as the result of arm's length bargaining." P. 540. The petitioners had expert economic evidence that the increase allowed by the escalation clause was much less than the rise in the value of gas from 1951 through 1954. P. 541. There was also evidence that the price sought "falls within the range of prices paid to other producers in the pricing area." P. 544. All of this was, of course, pertinent.

The Commission sustained the examiner's conclusion, however, agreeing with him that since petitioners "have wholly failed to offer any evidence respecting their investment in plant or their costs of operations,"[25] a fair balance could not be struck between producers and consumer interest.

The decisions, we think, support this view. As the Supreme Court said in *Federal Power Commn.* v. *Natural Gas Pipeline Co.*, 315 U. S. 575, 586:

> "The Constitution does not bind rate-making bodies to the service of any single formula or combination of formulas. Agencies to whom this legislative power has been delegated are free, within the ambit of their statutory authority, to make the pragmatic adjustments which may be called for by particular circumstances. Once a fair hearing has been given, proper findings made and other statutory requirements satisfied, the courts cannot intervene in the absence of a clear showing that the limits of due process have been overstepped. If the Commission's order, as applied to the facts before it and viewed in its entirety, produces no arbitrary result, our inquiry is at an end."

A concurrence highlights this conclusion, p. 604:

> "The rule of *Smyth* v. *Ames*, as construed and applied, directs the rate-making body in forming its

[25] Id., 544 and 521. See note 24, supra.

> judgment as to 'fair value' to take into consideration various elements—capitalization, book cost, actual cost, prudent investment, reproduction cost. . . . The rule of *Smyth* v. *Ames*, as interpreted and applied, means merely that all must be considered. What, if any, weight shall be given to any one, must practically rest in the judicial discretion of the tribunal which makes the determination."

This statement as to the power of the Commission was repeated in *Federal Power Commn.* v. *Hope Gas Co.*, 320 U. S. 591, 602.

What the Commission has done is to say that petitioners must make a showing as to its operations. It seems to us reasonable to make such a requirement. The primary aim of the Natural Gas Act is "to protect consumers against exploitation at the hands of natural gas companies."[26] One aid to such an aim is to weigh the needs of the gas companies by an examination of its costs and profits. What better test could there be as to the reasonableness of existing or proposed rates to a company than a careful analysis of the evidence as to its recent earnings?[27] That is one of the elements of any rate-testing method.

Third. The petitioner Continental Oil Company objects to the proceeding by the Commission under § 4 (e), see notes 2 and 6, supra, on the special ground that the section requires "a statement in writing of its reasons" for such suspension. Continental argues that the statement made in the case at bar was only a "hypothetical statement copied almost verbatim from statutory language," that the corporation could not know what objections to

[26] Id., at 610.

[27] Cf. Ilel Oil Corp. v. Federal Power Commn., 255 F. 2d 548; City of Detroit v. Federal Power Commn., 230 F. 2d 810, 818; Union Oil Co. of California, 16 F.P.C. 100, 108-110.

meet. Subject to all reservations and protests as to the necessity for filing, Continental filed its "Change in Rate Schedule," pointing out that it was a "fixed escalation" clause of the contract, providing for a half cent increase per MCF. It asserted that the price was reached by arm's length bargaining, that other less available gas sold for more and that the escalation was reasonable. Tables showed the volume sold and money received based on present and increased price. Nothing was shown as to the expenses of the operation.

The Commission ordered a public hearing and suspended the increase pursuant to sections 4 and 15 of the Natural Gas Act and the Commission's Rules and Regulations, 18 CFR, Chap. 1, after finding:

> "The increased rates and charges proposed in the aforesaid filing [have] not been shown to be justified, and may be unjust, unreasonable, unduly discriminatory, or preferential, or otherwise unlawful."

The rules, §154.63 (3), give detailed instructions for data to be submitted with changes in a tariff too long for inclusion here but covering sales volume, revenue, working capital, expenses, and a recent twelve-months balance sheet. The burden is upon the applicant for an increase under § 4. We have no doubt that the order of suspension fully advised petitioners of the information required to establish the necessity for the increase. Cf. *Phillips Petroleum Co.* v. *Federal Power Commn.*, 227 F. 2d 470, 474. The decision of the examiner discussed above certainly was specific. No reason appears why the petitioners could not meet the requirements.

Fourth. Another contention of Continental may be shortly answered. This contention is that another independent producer in the same field, Gulf Oil Corporation, selling to the same buyer under the same contract, filed on February 4, 1955, a change in Rate Schedule asking for similar reasons the approval of the perodic escalation

clause as applied to it. On April 6, Gulf was advised that the raise requested had become effective as requested.

Obviously, any such arbitrary differentiation without any distinction as to the proceeding is not permissible.[28] It is clear to us, however, that the differentiation under the circumstances it occurred cannot be made a reason for reversing the Commission's order in these cases. The Commission's explanation is this. The Gulf increase rate would produce an estimated $238 per year total. The approval was routine. As soon as the Gulf approval was brought to the Commission's attention, the Commission instituted an investigation which it consolidated with petitioners' proceeding. This so-called discrimination is not the type that requires like handling of other similar applications for rate increases. A motion to correct the Gulf order would be adequate. Cf. *American Trucking Assn. v. Frisco Co.*, 358 U. S. 133, 140.

Fifth. Finally we consider a motion filed in case No. 14581 by the respondent, the Commission, to dismiss all petitioners except Pan American Petroleum Corporation for want of jurisdiction in this court to consider the petition for review as to them because these petitioners had not been parties to the Commission proceedings. Court review of Commission orders is governed by § 19 of the Act.[29]

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[28] Cf. Atlantic Seaboard Corp. v. Fed. Power Commn., 201 F. 2d 568, 570.

[29] 15 U.S.C. § 717r. Rehearings; court review of orders

"(a) Any person, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this chapter to which such person, State, municipality, or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. . . . No proceeding to review any order of the Commission shall be brought by any per-

This proceeding was started by the application of Stanolind, now Pan American, for the change in the rate schedule discussed above. The record shows that the letter of transmittal was headed as follows:

> "Change in Rate Schedule (Docket No. G-4452) of Stanolind Oil and Gas Company et al for sale of Natural Gas as an Independent Producer under Section 4 of the Natural Gas Act, in accordance with Federal Power Commission Order No. 174-B, issued December 17, 1954 (Stanolind No. 19,446)."

The first paragraph read:

> "1. Pursuant to the requirements of Part 154 of Subchapter E, Regulations under the Natural Gas Act, Chapter I of Title 18, Code of Federal Regulations, as amended by Federal Power Commission Order No. 174-B, issued December 17, 1954, under Docket No. R-138, and particularly pursuant to Section 154.94 of said Regulations, the undersigned, Stanolind Oil and Gas Company, individually, and as operator of the jointly-owned properties involved herein, hereby gives notice to the Federal Power Commission and to the public of a change in the rates and charges presently in effect with respect to the sale of natural gas to the purchaser listed in Exhibit 'B', attached hereto. . . ."

So far as pertinent, the eighth and ninth paragraphs read:

> "8. This change in rate schedule not only relates to Stanolind Oil and Gas Company's interest in the gas covered by said gas sales contract, but said change in rate schedule is also being filed for the benefit

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son unless such person shall have made application to the Commission for a rehearing thereon. . . .

"(b) Any party to a proceeding under this chapter aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia. . . ."

and in behalf of all nonoperators whose respective shares of the gas produced from jointly-owned properties operated by Stanolind have been sold under the contract referred to herein by Stanolind, as their agent, because of their failure to dispose of the same, to the extent that such nonoperators elect in writing to concur herein or to adopt this filing of a change in rate schedule as their own.

"9. Pursuant to the provisions of Clause (1) of Paragraph (b) of Sec. 154.91 of Order 174-B, this change in rate schedule is also being filed by Stanolind, as operator of the jointly-owned properties covered by said rate schedule, for and on behalf of all nonoperators owning interests in said properties. Attached hereto as Exhibit 'D' is a list of (a) all persons having working interests involved in the sale of natural gas covered by this filing, (b) the parties to the operating agreements covering the respective jointly-owned properties and (c) a statement of the respective interests of such parties in said properties. To the extent that any of said persons or parties has heretofore filed or hereafter files for itself with respect to the change in rate covered hereby, then this filing shall not apply to it or to its interests in the gas produced from said jointly-owned properties. . . ."

Apparently there was an operating agreement for the various units that have been formed for selling gas under which the operator, Pan American, sells the gas of the units and attends to the management of the contract.

The record shows the method of selling generally:

"Q. What about that? Who were you negotiating for? A. For Stanolind.

"Q. The contract you were attempting to draw was for Stanolind only? What about Continental? A. Continental was in on the negotiations for themselves.

"Q. As to the other persons in the field, you were not at that time acting for them. Is that right? A. In a manner of speaking we were. Naturally as operators of the properties, it was our responsibility to make as good arrangements as possible for the disposition of the production.

"Q. Then the operating agreement in the field had been entered into prior to these negotiations or during the course of them? A. There were operating agreements. There is an operating agreement on each unit. Some of those were in effect at the time." R. 73.

"Q. You stated a while ago there is an operating agreement for each of the various units in the field. Is that correct? A. Yes, sir.

"Q. Under those operating agreements, does Stanolind, if it is the operator, have the right to sell anybody's gas except Stanolind's? A. Only for a period up to and not in excess of one year, and only in the absence of their election to take it themselves." R. 120.

All the petitioners here were specifically named in the application for rehearing. The application opened, "On behalf of the Episcopal Theological Seminary," then following other named parties, "comes now Pan American Petroleum Corporation (Pan American), by its attorneys, and pursuant to Section 19 (a) of the Natural Gas Act, files this Application for Rehearing." No one under § 19 could file an application for rehearing unless they were a party. No one except Pan American had been a party to the original hearing. Therefore, the inclusion of their names in the application for rehearing was merely descriptive. We do not think that under § 19 any gas producer selling under the Pan American contract could be a petitioner on appeal who had not been a party in the proceeding before the Commission prior to the order refusing the escalation. Cf. *Federal Power Commn.* v. *Colorado Interstate Gas Co.*, 348 U. S. 492, 497; *Sun Oil Co.* v. *Federal Power Commn.*, 256 F. 2d 233, 239.

The practical necessity for allowing the operator to represent the many producers who make up the supply for the sale to the pipe lines led the Commission to adopt October 4, 1956, regulations since the beginning of these proceedings.[30] This section allows the operator who sells

[30] 18 CFR 154.91.

for producers to make the rate schedule filings and changes. As we think the petitioners whom the respondent seeks to strike were not parties to these proceedings before the Commission, we need not determine the effect of this October 4, 1956, amendment.

What we do determine on this motion to strike is that none of the petitioners except Pan American was a party to the Commission proceeding or was entitled to appeal under the provisions of Section 19 of the Natural Gas Act.

It follows that the motion to dismiss all petitioners except Pan American Petroleum Corporation for lack of jurisdiction in this court is sustained.

It further follows that the order of the Federal Power Commission of April 14, 1958, should be affirmed.

It is so ordered.

UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

September Term, 1958

No. 14,581

EPISCOPAL THEOLOGICAL SEMINARY OF THE SOUTHWEST, ET AL., *Petitioners*,

v.

FEDERAL POWER COMMISSION, *Respondent*.

September Term, 1958

No. 14,588

CONTINENTAL OIL COMPANY, *Petitioner*,

v.

FEDERAL POWER COMMISSION, *Respondent*.

On Consolidated Petitions for Review of Orders of the Federal Power Commission, and on Motion of Respondent in No. 14,581 to Dismiss Petition for Review.

Before: Mr. Justice Reed, retired, and Prettyman, Chief Judge, and Fahy, Circuit Judge.

Judgment

These cases came on to be heard on the record from the Federal Power Commission and on respondent's motion to dismiss as to all petitioners in No. 14,581 for want of jurisdiction except Pan American Petroleum Corporation and petitioners' answer thereto, and were argued by counsel.

ON CONSIDERATION WHEREOF, it is ordered and adjudged by this court (1) that in No. 14,581 respondent's motion to dismiss for lack of jurisdiction is granted as to all petitioners except as to Pan American Petroleum Corpora-

tion, and (2) that in Nos. 14,581 and 14,588 the order of the Federal Power Commission dated April 14, 1958, on review is affirmed.

Per Mr. Justice Reed.

Dated: June 18, 1959

APPENDIX B

The Provisions of the Fifth Amendment to the Constitution of the United States. U.S. Const., Amend. V, are as Follows:

"No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

The Pertinent Provisions of the Natural Gas Act of June 21, 1938, c. 556, 52 Stat. 821, 15 U.S.C. 717, are as Follows:

RATES AND CHARGES; SCHEDULES; SUSPENSIONS OF NEW RATES

Sec. 4.

(a) All rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) No natural-gas company shall, with respect to any transportation or sale of natural gas subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or, (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission within such time (not less than sixty days from the date this act takes effect) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulations, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, or State commission, or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reason for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect: *Provided*, That the Commission shall not have authority to suspend the rate, charge, classification, or service for the sale of natural gas for resale for industrial use only; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period, on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective the Commission may, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a

rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible. [52 Stat. 822 (1938); 15 U.S.C. 717e (1946)].

FIXING RATES AND CHARGES; DETERMINATION OF COST OF PRODUCTION OR TRANSPORTATION

Sec. 5.

(a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however*, That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

(b) The Commission upon its own motion, or upon the request of any State commission, whenever it can do so without prejudice to the efficient and proper conduct of

its affairs, may investigate and determine the cost of the production or transportation of natural gas by a natural-gas company in cases where the Commission has no authority to establish a rate governing the transportation or sale of such natural gas. [52 Stat. 823 (1938); 15 U.S.C. 717d (1946)].

REHEARING; COURT REVIEW OF ORDERS

SEC. 19.

(a) Any person, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this act to which such person, State, municipality, or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. The application for rehearing shall set forth specifically the ground or grounds upon which such application is based. Upon such application the Commission shall have power to grant or deny rehearing or to abrogate or modify its order without further hearing. Unless the Commission acts upon the application for rehearing within thirty days after it is filed, such application may be deemed to have been denied. No proceeding to review any order of the Commission shall be brought by any person unless such person shall have made application to the Commission for a rehearing thereon.

(b) Any party to a proceeding under this act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of

such petition shall forthwith be served upon any member of the Commission and thereupon the Commission shall certify and file with the court a transcript of the record upon which the order complained of was entered. Upon the filing of such transcript such court shall have exclusive jurisdiction to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which is supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U.S.C., title 28, secs. 346 and 347).

(c) The filing of an application for rehearing under subsection (a) shall not, unless specifically ordered by the Commission, operate as a stay of the Commission's order. The commencement of proceedings under subsection (b) of

this section shall not, unless specifically ordered by the court, operate as a stay of the Commission's order. [52 Stat. 831 (1938); 15 U.S.C. 717r (1946)]

The Pertinent Provisions of the Administrative Procedure Act of June 11, 1946, c. 324, 60 Stat. 241; 5 U.S.C. § 1009, are as follows:

Sec. 10 Except so far as (1) statutes preclude judicial review or (2) agency action is by law committed to agency discretion—

(a) Right of review.—Any person suffering legal wrong because of any agency action, or adversely affected or aggrieved by such action within the meaning of any relevant statute, shall be entitled to judicial review thereof.

(b) Form and venue of action.—The form of proceeding for judicial review shall be any special statutory review proceeding relevant to the subject matter in any court specified by statute or, in the absence or inadequacy thereof, any applicable form of legal action (including actions for declaratory judgments or writs of prohibitory or mandatory injunction or habeas corpus) in any court of competent jurisdiction. Agency action shall be subject to judicial review in civil or criminal proceedings for judicial enforcement except to the extent that prior, adequate, and exclusive opportunity for such review is provided by law.

(c) Reviewable Acts.—Every agency action made reviewable by statute and every final agency action for which there is no other adequate remedy in any court shall be subject to judicial review. Any preliminary, procedural, or intermediate agency action or ruling not directly reviewable shall be subject to review upon the review of the final agency action. Except as otherwise expressly required by statute, agency action otherwise final shall be final for the purposes of this subsection whether or not there has been presented or determined any application for a declaratory

order, for any form of reconsideration, or (unless the agency otherwise requires by rule and provides that the action meanwhile shall be inoperative) for an appeal to superior agency authority.

(d) Interim Relief.—Pending judicial review any agency is authorized, where it finds that justice so requires, to postpone the effective date of any action taken by it. Upon such conditions as may be required and to the extent necessary to prevent irreparable injury, every reviewing court (including every court to which a case may be taken on appeal from or upon application for certiorari or other writ to a reviewing court) is authorized to issue all necessary and appropriate process to postpone the effective date of any agency action or to preserve status or rights pending conclusion of the review proceedings.

(e) Scope of Review.—So far as necessary to decision and where presented the reviewing court shall decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of any agency action. It shall (A) compel agency action unlawfully withheld or unreasonably delayed; and (B) hold unlawful and set aside agency action, findings, and conclusions found to be (1) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; (2) contrary to constitutional right, power, privilege, or immunity; (3) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; (4) without observance of procedure required by law; (5) unsupported by substantial evidence in any case subject to the requirements of sections 7 and 8 or otherwise reviewed on the record of an agency hearing provided by statute; or (6) unwarranted by the facts to the extent that the facts are subject to trial de novo by the reviewing court. In making the foregoing determinations the court shall review the whole record or such portions thereof as may be cited by any party, and due account shall be taken of the rule of prejudicial error.

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No. 505

In the Supreme Court of the United States

October Term, 1959

PAN AMERICAN PETROLEUM CORPORATION, ET AL.,

v.

FEDERAL POWER COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL POWER COMMISSION IN OPPOSITION

[redacted]

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In the Supreme Court of the United States

OCTOBER TERM, 1959

No. 405

PAN AMERICAN PETROLEUM CORPORATION, PETITIONER

v.

FEDERAL POWER COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE FEDERAL POWER COMMISSION IN OPPOSITION

OPINIONS BELOW

The orders of the Federal Power Commission (R. 334–342, 380–386) are reported at 19 F.P.C. 519 and 917. The opinion of the Court of Appeals for the District of Columbia Circuit (Pet. App. 1a–21a) is reported at 269 F. 2d 228.

JURISDICTION

The judgment of the Court of Appeals was entered on June 18, 1959 (Pet. App. 22a). The petition for a writ of certiorari was filed on September 14, 1959. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1) and Section 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

QUESTION PRESENTED

The Federal Power Commission held that petitioner had not sustained its burden of showing the reasonableness of its proposed increased rate because of its failure to offer any evidence with respect to its costs or revenue requirements. The court below held that the Commission had not abused its discretion in requiring cost evidence in this case. The question presented is whether the Commission had in fact exercised its discretion in requiring such evidence in this case, or whether the Commission was applying a statutory or constitutional rule of law that such evidence is required in all independent-producer rate cases.

STATUTES INVOLVED

The applicable portions of the Natural Gas Act are set forth in petitioner's appendix at pp. 23a–29a.

STATEMENT

Petitioner is an independent producer of natural gas which sells gas from Woodlawn Field, Texas, to an interstate pipeline, Mississippi River Fuel Corporation, under a contract entered into in 1951 for a term of twenty years (Pet. App. 2a). The contract provides for periodic escalations in price (Pet. App. 2a).

In October 1954, petitioner filed this contract with the Federal Power Commission as its FPC Gas Rate Schedule No. 31, pursuant to the requirements of the Natural Gas Act, as construed in this Court's decision in the *Phillips* case,[1] and the Commission's No.

[1] *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672.

174 series of orders [2] implementing that decision (Pet. App. 2a–3a). The rate in effect on June 7, 1954 (the date of the *Phillips* decision, which was adopted by the Commission for commencing regulation of independent producers under the Act), was 13¢ per Mcf. In March 1955, petitioner filed a notice of change in the rate, effective April 3, 1955, from 13 to 13.5¢ per Mcf, in accordance with the escalation clause in the contract (Pet. App. 4a, R. 186). The Commission, pursuant to Section 4(e) of the Act, ordered a hearing on the lawfulness of the increased rate and suspended it until September 3, 1955, when it was made effective subject to refund if not found justified (R. 247, 270).

In the hearing before a Commission trial examiner,[3] petitioner, in order to show the lawfulness of its increased rate, relied on evidence merely showing that the 13.5¢ per Mcf rate was not higher than prices being charged by other producers in the general area of the sale and not excessive in comparison to the prices of competitive fuels; and also that the increase would have an inconsequential effect on the price of natural gas to the ultimate consumer.[4] Petitioner did not

[2] 18 C.F.R. (1958 Cum. Supp.) 154.91 *et seq.*

[3] The proceeding also involved the rate increase of Continental Oil Company which, as a co-signatory with petitioner, had filed the same contract and notice of change. Continental offered the same type of evidence as petitioner.

[4] As found by the examiner, the testimony shows that the contract price when negotiated was the highest price that had been negotiated for sale of gas in Texas and was the highest price paid for gas by Mississippi River Fuel Corporation to anyone in the Woodlawn Field at the time of the hearing (R. 302).

offer any evidence as to its costs or as to the need for the additional revenue which would be provided by the suspended rate. The Commission staff did not present any evidence, but moved to dismiss the rate increase proposal on the ground that petitioner had not discharged its statutory burden of establishing the reasonableness of its higher rate. (R. 303–306.)

The hearing examiner recommended that the application be dismissed, finding that petitioner failed to introduce any form of cost evidence and had "wholly failed" to sustain its burden of establishing the reasonableness of the proposed increased rate (R. 311–312). In reaching this conclusion, the examiner relied upon *City of Detroit* v. *Federal Power Commission,* 230 F. 2d 810 (C.A.D.C.), certiorari denied, 352 U.S. 829, and the Commission's decision in *Union Oil Co.,* 16 F.P.C. 100 (subsequently affirmed on this point but remanded on a procedural point, *Bel Oil Corp.* v. *Federal Power Commission,* 255 F. 2d 548 (C.A. 5), certiorari denied, 358 U.S. 804). The Commission affirmed, adopting the examiner's decision (R. 339). In applying for a rehearing, petitioner contended, *inter alia,* that the Commission had erred in concluding that petitioner's "failure to adduce evidence of cost of service or revenue requirements as a point of departure resulted in a failure to sustain the justness and reasonableness of * * * proposed increased rates under *City of Detroit* v. *Federal Power Commission,* 230 F. 2d 810" (R. 381). The Commission rejected this contention, stating that a complete answer was provided by the Fifth Circuit's statement in *Bel Oil, supra,* that, "without deciding that the rate-

base method is essential in every rate case" (255 F. 2d at 553), evidence of unregulated field prices when coupled only with testimony that the price must be high enough to provide incentive for exploration and development of new sources of supply is not sufficient to permit the Commission to approve a rate as just and reasonable.

The court below affirmed, holding that the Commission had acted reasonably in requiring petitioner to make a showing as to its operations and earnings (Pet. App. 15a).

ARGUMENT

Petitioner contends (1) that the Federal Power Commission erroneously concluded that, in the absence of conventional cost-of-service evidence, it could not, as a matter of law, find that petitioner's increased rate was just and reasonable, and (2) that the court below exceeded its statutory power by affirming the Commission not on the statutory and constitutional grounds which petitioner says were relied on by the Commission but only on the basis that the Commission, in its discretion, could require cost evidence as a starting point in this particular case. Both contentions are based on the single premise that the Commission, in requiring cost-of-service evidence, was not exercising its discretion but instead believed it was under a statutory and constitutional compulsion to require such evidence in all independent-producer rate cases (Pet. 18, 20, 21–23). There is no foundation for this premise and accordingly no occasion for review by this Court.

The Commission's order denying petitioner's application for rehearing makes it clear, we submit,

that the Commission did not hold that cost-of-service evidence must always be presented by independent producers in support of proposed increased rates. The Commission found only that the evidence here, which related solely to the market value or "fair field price" of the gas sold by petitioner (R. 298–311), was not sufficient to permit a finding that this proposed rate was just and reasonable (R. 383). And the Commission held that the Fifth Circuit's reasoning in *Bel Oil Corporation* v. *Federal Power Commission*, 255 F. 2d 548, certiorari denied, 358 U.S. 804, where (as here) the producers refused to offer cost evidence to establish the reasonableness of proposed increased rates, provided a full answer to the contention that cost evidence should not be required. It quoted the following language from *Bel Oil* (R. 382):

> * * * We do not hold that evidence of field price is irrelevant. We do hold that evidence of unregulated prices in the field is not sufficient to warrant a finding by the Commission that a price comparable to them is just and reasonable within the intendment of the Natural Gas Act. Neither is evidence of the field price when coupled with the opinion of experts that the price must be high enough to provide an incentive for exploration and development of new sources of supply.
>
> * * * Without deciding that the rate-base method is essential in every rate case, we agree that the Commission did not have sufficient evidence before it to approve these rates as just and reasonable. [255 F. 2d at 553]

Moreover, as recognized by the Fifth Circuit in the *Bel Oil* case and in *Gulf Oil Corp.* v. *Federal Power Commission*, 255 F. 2d 556, the Commission had recognized in *Pan American Petroleum Corp., et al.*, 19 F.P.C. 463, that conventional cost-of-service evidence was not required in all independent-producer rate cases.

It is apparent, therefore, that in holding that without any evidence of its costs this petitioner had not justified its proposed rate, the Commission was exercising its discretion and not, as petitioner contends, acting in the belief that such evidence was required as a matter of law in all independent-producer cases.

We note, finally, that petitioner does not challenge the Commission's discretionary power to require cost-of-service evidence in regulating producer rates. Indeed, this Court has made it clear in *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591, and *Colorado Interstate Gas Co.* v. *Federal Power Commission*, 324 U.S. 581, that the formula employed in setting gas rates is a matter within the discretion of the Commission and that the Commission, if it chooses, may employ a cost-of-service standard in setting gas rates. The Court pointed out explicitly in the latter case (324 U.S. at 601) that:

> We do not say that the Commission lacks the authority to depart from the rate-base method. We only hold that the Commission is not precluded from using it. * * *

See also *Federal Power Commission* v. *Natural Gas Pipeline Co.*, 315 U.S. 575, 586.

CONCLUSION

For these reasons, it is respectfully submitted that the petition for a writ of certiorari should be denied.

J. LEE RANKIN,
Solicitor General.
GEORGE COCHRAN DOUB,
Assistant Attorney General.
SAMUEL D. SLADE,
Attorney.

WILLARD W. GATCHELL,
General Counsel,
HOWARD E. WAHRENBROCK,
Solicitor,
W. RUSSELL GORMAN,
Assistant General Counsel,
PETER H. SCHIFF,
Attorney,
Federal Power Commission.

OCTOBER, 1959

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1959

No. 405

PAN AMERICAN PETROLEUM CORPORATION, *Petitioner,*

v.

FEDERAL POWER COMMISSION, *Respondent.*

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

PETITIONER'S REPLY TO BRIEF FOR THE FEDERAL POWER COMMISSION IN OPPOSITION

W. W. HEARD
JOHN F. JONES
Pan American Petroleum Corporation
P. O. Box 591
Tulsa 2, Oklahoma

WILLIAM J. GROVE
CARROLL L. GILLIAM
Dow, Lohnes and Albertson
600 Munsey Building
Washington 4, D. C.

Attorneys for Petitioner

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PETITIONER'S REPLY TO BRIEF FOR THE FEDERAL POWER COMMISSION IN OPPOSITION

INTRODUCTORY STATEMENT

Opposition to review of this case has been predicated solely upon one of the grave errors which have deprived Petitioner and others of due process of law—substitution of decisional grounds during the course of judicial review. Of equally grave import, in this Court, is the fact that statements now filed on behalf

of the Federal Power Commission are such a departure from the expression of its conclusions of law in orders and in the courts during the past four years, that a confession of error in the instant case should be required.

Petitioner has been subjected to an administrative sleight-of-hand—under what "shell" is the "pea"? At considerable expense Petitioner and others have been the subject of a protracted rate proceeding before a federal agency. Before the agency itself, the primary issue was whether "cost-of-service" evidence was required by the statute involved and by the Constitution. Petitioner took the position that it was not. The legal staff of the Commission took the position that it was. First the Examiner and then the Commission held that, as a matter of law, the statute and the Constitution required "cost-of-service" evidence (R. 3308-3309, 3433). Unquestionably, the Commission's holding was that it had no discretion in the matter. In fact, the Commission specifically refused to state what its holding would have been had it determined that neither the statute nor the Constitution required "cost-of-service" evidence (R. 3498-3499).

After challenging at every opportunity the Commission's construction of the statute and the Constitution, Petitioner was, for the first time, met in the Court of Appeals with the contention that it was not the statute or the Constitution that required "cost-of-service" evidence, but the Commission in its "discretion." Clearly, this was not the basis of the Commission's decision.

For over five years the most burning issue before the Commission has been whether the statute and the Constitution required consideration of "cost-of-service"

evidence in independent gas producer rate cases. The Staff of the Commission, including its legal staff, has consistently contended that they do.[1] Independent producers have consistently contended that, because of the unique characteristics of their business and legal precedent, there is no such "statutory" or "constitutional" requirement. In public statements various members of the Commission have, from time to time, expressed the opinion that the rates of independent producers should not be regulated on a "conventional cost-of-service" basis.[2] Yet, in this case, and in practically every other decision it has rendered regarding this question, the Commission itself has tenaciously held that the statute and the Constitution required "conventional cost-of-service" evidence in independent producer rate cases. All of this is, of course, well known to the Commission's legal staff.

In the Court of Appeals, Petitioner objected to the shifting by the Commission's attorneys from the Commission's holding that the statute and the Constitution required the result it had reached. Petitioner renews that objection here.

Regardless of the erroneous statements contained in the Brief in Opposition to the granting of a writ, it is of public importance that the Commission be given an opportunity to determine *for itself* whether, as a matter of informed discretion, it should require "cost-of-service" evidence in independent gas producer rate cases. As long as it is consistently advised by its Staff that it has no discretion in the matter because the stat-

[1] See footnote 23, p. 25, of our Petition.

[2] See, *e.g.* Connole, "General Considerations: A Nation's Natural-Gas Pains," 44 Geo. L. J. 555 (1956).

nte and the Constitution require such evidence, and as long as the Commission acts upon that advice in a given case, it can hardly be said that it has exercised its discretion in that case. The posture of this case is now such that failure to grant this Petition for Writ of Certiorari will prevent the Commission itself from ever having an opportunity to exercise its discretion with respect to this question.

The shifting of grounds upon which decisions are based, which is beyond mere differences between opposing counsel in interpretation of language in administrative orders, also improperly forestalls judicial review. The pattern that has been followed here—deprivation of rights *solely* by statutory and constitutional construction, followed by judicial approval of such action on entirely new and different grounds of "discretion"—inevitably leads to unrestrained, unreviewable administrative power.

Additionally, inconsistencies between the statements filed herein and the positions heretofore taken on behalf of the Commission in the courts have obviously interjected more confusion into the hundreds of pending proceedings under Section 4(e) of the Natural Gas Act. These inconsistencies also demonstrate, at the very least, the need for clarification by this Court as to statutory or constitutional limitations upon Commission power in rate review proceedings under Section 4(e).

ARGUMENT

I. There is no foundation for the characterization of the Commission's actions that is set forth in the Brief in Opposition. In addition to misstating the

procedural history of the instant case,[3] the Brief opposes review with the single, erroneous proposition that the Commission has *not* made conclusions of law that statutory and constitutional requirements preclude decision in a proceeding of limited scope under Section 4(e) unless "conventional rate base, cost-of-service" evidence is presented. As the entire gas industry is aware, this simply is not the case. Quite to the contrary, the sixty-four producers here and scores of other persons in numerous proceedings have been denied contract rights solely upon the basis of the explicit conclusions of law challenged in the court below and outlined in our Petition in this Court.

What has led to this posture of the instant case, to the widespread confusion in pending cases, and to questions of propriety of the assertions in the Brief in Opposition, may be easily demonstrated by only the briefest reference to the Commission orders in this case and to the cases cited in the Brief in Opposition:

1. While the instant proceeding was before an Examiner, the Commission itself held on December 6, 1956, in *Re Union Oil Company of California*, 16

[3] Contrary to assertions in the Brief in Opposition, p. 4, during the proceeding before the Commission, the Commission's Staff *did* present evidence upon the question of commodity value and value to the purchaser. The Staff did *not* file a motion "to dismiss the rate increase." In findings adopted by the Commission, the Staff's presentation was rejected as unprobative (R. 3303, 3306). The case was decided, *not* upon motion to dismiss, but in the normal course with exceptions and briefing on *issues of law* by both the Staff and the producers (R. 3433). As to the characterizations of the evidence presented (Brief in Opposition at pp. 3-4), reference is made to the extensive showings appearing at R. 61-65, 72, 76-84, 396, 405-16, 1829-1836, 1870-1892, 2200, 2203, 2221, 2521, 2526, 2527, 3306, and to the findings at R. 3302-3, 3305-08 and to the summary statement at pages 7-9 in our Petition herein.

F.P.C. 100 (1956), (an independent producer proceeding of limited scope under Section 4(e) of the Act) that both the Act and the Constitution precluded decision by it unless "conventional, rate base cost-of-service" evidence appeared in the record. Illustrative of the Commission's conclusions of law are the following (emphasis supplied):

> "Upon careful consideration of the entire record, we find the applicants have failed to submit evidence on which we could determine that, *as a matter of law*, the rates here in question are just and reasonable." (16 F.P.C. at 105).
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>
> "We think it is plain from the language of the *City of Detroit* case, supra, that *the value method used alone*, as proposed by the applicants, is *not a method open to us within our delegated power*." (16 F.P.C. at 110)
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> * * * * * * * * *
>
> "It is impossible to meet the *requirements of either the Act or the Constitution* unless we can determine the revenue requirements of the industry we must regulate and the effect of the *rate in question* on its earning capacity." (16 F.P.C. at 111)
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> * * * * * * * * *
>
> "Based upon the foregoing analysis . . . we find that the applicants have failed, *as a matter of law*, to establish that the 17-cent rates are just and reasonable." (16 F.P.C. at 111)
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> * * * * * * * * *

2. Two months thereafter, on February 8, 1957, the Examiner in the instant case stated the controlling question before him to be that raised by the conclusions of law expressed in the *Union Oil Company* proceeding (R. 3308):

> "... 'The central issue presented is one of constitutional requirements and of our statutory power.'"

The Examiner then clearly predicated his ultimate conclusion upon the Commission's conclusions of law in the *Union Oil Company* proceeding (R. 3309):

> "... here, too, 'It is impossible to meet the requirements of either the Act or the Constitution unless we can determine the revenue requirements **of the industry we must regulate** and the effect of the rate in question on its earnings capacity.'"

3. While the instant case was pending before the Commission itself on Exceptions by the producers and the Staff, and while the *Union Oil Company* decision was pending on review in the Court of Appeals for the Fifth Circuit, the Commission, on April 4, 1958, issued its opinion in the distinct and unrelated case reported as *Re Pan American Petroleum Corporation, et al.*, 19 F.P.C. 463. There, the Commission apparently and correctly concluded that where but one of many of a producers' sales prices was in issue under Section 4(e), "conventional cost-of-service evidence was not required."

4. Notwithstanding this holding on April 4, 1958, only ten days later, on April 14, 1958, the Commission issued its final order in the instant case, and, without explanation, returned to the conclusions of law it had adopted in the *Union Oil Company* case (R. 3432). As the record herein shows, the Commission explicitly adopted, as its own, the statements of the "central issue" and conclusions of law expressed by the Examiner (R. 3433, 3435). The Commission just as explicitly referred to its conclusions of law in the *Union*

Oil Company case and to *City of Detroit* v. *Federal Power Commission*, 230 F. 2d 810 (D.C. Cir. 1955) as controlling. (R. 3435):

> "We conclude that the companies have not shown their proposed increased rates are justified, nor can they until they meet the *requirements of these decisions.*" (Emphasis supplied).

5. Nine days thereafter, on April 23, 1958, the Court of Appeals for the Fifth Circuit issued its opinion and order of remand in the *Union Oil Company* case, *sub nom. Bel Oil Corporation, et al* v. *Federal Power Commission*, 255 F. 2d 549 (1958). Having the *Pan American* opinion of April 4, 1958, before it, but *not* the opinion of April 14, 1958 in the instant case, that Court assumed that on April 4, 1958, the Commission had abandoned the sweeping conclusions of law expressed in the *Union Oil Company* opinion. (See 255 F. 2d at 553).

6. Such an assumption was however, clearly unwarranted. In pending matters, the Commission continued to hold that there was a legal requirement for presentation of "conventional rate base, cost-of-service" evidence, regardless of the scope of the proceeding.[4] On June 6, 1958, on precisely those grounds, it denied rehearing in the instant case. Contrary to the mischaracterization of the order denying rehearing in the Brief in Opposition herein, that order was a reiteration of the conclusions of law in the *Union Oil Company* case and in the final order in the instant case. The Commission clearly held (R. 3498):

[4] See *Re Humble Oil & Refining Company*, 19 F.P.C. 697 (1958); *Re H.L. Hunt*, 19 F.P.C. 748 (1958); *Re Sun Oil Company*, 19 F.P.C. 800 (1958); *Re Sun Oil Company*, 19 F.P.C. 973 (1958).

> "We do not have sufficient evidence here, any more than *we had* in the Bel Oil [Union Oil Company] case, to approve the proposed increased rates as just and reasonable *under the law*. * * * *Under City of Detroit*, the value method used alone is not sufficient to determine just and reasonable rates." (Emphasis supplied).

And, again, the Commission repeated its adoption of the conclusions of law set forth in the Examiner's Decision (R. 3498).

7. Similarly, the Commission continued to urge upon the Court of Appeals for the Fifth Circuit the same conclusions of law advanced in the *Union Oil Company-Bel Oil Corporation* case. As that Court noted on February 20, 1959 in *Forest Oil Corporation* v. *Federal Power Commission*, 263 F. 2d 622, 625 (5th Cir. 1959):

> "Nevertheless in the briefs filed in this case and the companion case . . . *the Commission does not deviate from its position taken before our Bel Oil opinion*. . . .
>
> * * * * * * * * *
>
> "The briefs still speak of cost of service or rate base proof." (Emphasis supplied)

8. Meanwhile, the instant case was before the Court of Appeals for the District of Columbia Circuit. With respect to the orders under review, the Commission's brief there stated:

> "Whether or not the Commission was *required* to *hold* 'cost' evidence necessary to petitioners' case, *under the controlling judicial authorities*, need not be decided. *The fact is, that the Commission did so hold* . . ."[2]

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[2] Brief for Respondent Federal Power Commission below, p. 10. Additional emphasis supplied.

Having thus recognized that the Commission *had* made conclusions of law, the Brief discussed the authorities. Upon the questions of law as to legal requirements for "conventional" presentation where but one of many rates is in issue, it was said, *inter alia*:

> "Neither the Natural Gas Act nor the cases give any support to the idea that where but one out of many rates is in question, the rate proponent may rely on market value (fair field price) of the gas and be absolved from the duty of presenting conventional rate-case evidence."[8]

But, upon the crucial question as to decision by the Court of Appeals, the Court was urged to affirm the orders *without* passing upon the validity of the conclusions of law which were the sole basis for the Commission's order, but upon the substituted grounds that the Commission had acted properly in an exercise of "discretion". (Brief in Opposition, p. 5).

9. Now, in the fifth year of this litigation, the Brief in Opposition in this Court, in addition to misstating procedural history of the instant case,[9] asserts that the Commission has *not* acted in the belief that "conventional cost-of-service" evidence was required "as matter of law" in proceedings of limited scope under Section 4(e).

An administrative agency, of course, can "change its mind," but if the change occurs during the course of review, the original order cannot be permitted to stand upon the basis of new grounds advanced so late in the case. Here, after four years of assertions of a con-

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[8] Ibid., p. 11.

[9] See fn. 3, *supra*.

trary view, the Commission apparently has now recognized that its previous holdings were completely erroneous, and that in proceedings under Section 4(e) of limited scope, neither the Act nor the Constitution impose a requirement that "conventional cost-of-service evidence" be submitted. Having thus abandoned the sole basis for the original order, the Brief on behalf of the Commission should not oppose review; there should be no reluctance to state a confession of error in the instant case. *Sunray Mid-Continent Oil Company* v. *Federal Power Commission*, 353 U.S. 944 (1957).

The Commission apparently has elected not to defend its conclusions of law in this Court. However, at the same time such an election is made here, the holding by the court below is cited in pending proceedings for the proposition that "the law" compels the Commission to use the "conventional cost-of-service method" in all cases.[*] Thus, the Brief in Opposition demonstrates the singular need for clarification and why all parties are left to speculate from one case to the next as to what constructions of the Act and the Constitution will be made by the Commission.

II. Finally, the Brief in Opposition also clearly exemplifies the importance of the second question herein—denial of the substance of review because of the shift of position by the Commission.

At the instance of the Commission, this Court has already granted a petition for a writ in *Federal Power Commission* v. *Shell Oil Corporation* (No. 170, Oct. Term, 1959; 28 L.W. 3098), wherein the Commission

[*] Compare the Brief in Opposition with the reference in footnote 23, page 25 of our Petition.

seeks a new restriction upon the scope of judicial review of its conclusions of law, and asserts error by a court of appeals which *did* independently review such conclusions. Of equal import to the industries over whom the Commission exercises jurisdiction, is the question of denial of due process by failure of a court to review explicit holdings and permitting shifting of decisional grounds. If, as the Commission urges, administrative agencies are to be permitted to apply conclusions of law in their proceedings and then, as has occurred here and in other cases, to avoid review of those conclusions by deliberately changing position during review, a[illegible] the review procedures so carefully prescribed by Congress will be nullified. Under the practice laid bare here, such error then may be compounded by reliance upon appellate decisions as affirming conclusions of law actually left unreviewed.

CONCLUSION

In this case alone, it has taken more than five years to move through the decision and review process—hearing, briefing, examiner's decision, exceptions, Commission consideration, Commission decision, application for rehearing, denial of rehearing, petitions for review, briefing, argument, appellate decision, and petition to this Court. Until the filing of the briefs in the Court of Appeals, the Commission's holding was clear, and even there, no clear concession of error on the questions of law appeared. But, at this late date, the Commission now speaks in this Court, and its words are again different. Apparently now conceding the validity of the very precedents the Commission has heretofore rejected, nevertheless the Brief still opposes review of Commission conclusions and of its denial of contract rights. It is urged that Petitioner

and others be left stripped, not only of rights, but also of the substance of a judicial scrutiny of the apparently discarded holdings that produced that result.

Aside from impropriety and prejudice to parties aggrieved in this and other cases by such an effort, this procedure effectively avoids all judicial review of the administrative process. No redress or correction of error is possible; administrative "discretion" to misconstrue the statute and the Constitution is wholly without limitation by any court, and even the semblance of due process of law disappears from federal administrative practice.

For the foregoing reasons and those stated in the Petition, it is respectfully submitted that this Petition for a Writ of Certiorari should be granted.

W. W. Heard
John F. Jones
Pan American Petroleum
Corporation
P. O. Box 591
Tulsa 2, Oklahoma

William J. Grove
Carroll L. Gilliam
Dow, Lohnes and Albertson
600 Munsey Building
Washington 4, D. C.
Attorneys for Petitioner

October, 1959.